88-264

Supreme Court, U.S.
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No. 87-

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1987

WILLIAM H. VOGT III,
Petitioner,

—against—

SHELDON ABISH and

MAHONEY, COHEN & CO., P.C.,
Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITON FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED FOR REVIEW

Whether the Court, in exercise of its supervisory authority over the regional circuits and the uniform construction and application of the Federal Rules of Civil Procedure by the inferior courts, should grant certiorari:

(1) To review the refusal of the court of appeals to review, on appeal or by mandamus,

(a) the failure of the district court to heed the requirements of Rule 60(b) for relieving a party from a final judgment;

(b) the district court's unlawful substitution of part (but not all) of the more lenient Rule 55(b) test for vacating a default prior to judgment, as the standard for setting aside a final judgment; and

(c) the district court's holding that it has power to vacate a final judgment for whatever reason it may see fit, because Rule 60(b)(6) allegedly confers upon it a "grand reservoir of equitable power to do justice."

(2) To review the court of appeals' frustration of petitioner's efforts to obtain timely and proper review of the district court's unlawful action in setting aside the final judgment against defendant Mahoney, Cohen,

(a) first, by dismissing petitioner's timely appeal of that issue, despite a hitherto unbroken line of Second Circuit precedent holding that district court action under Rule 60(b) be reviewed by appeal, rather than by mandamus;

(b) then by denying petitioner's timely application for a writ of mandamus filed after his appeal had been dismissed, which sought to confine the district court to lawful exercise of its jurisdiction and rescind its improper vacature of the final judgment against defendant Mahoney, Cohen.

(3) To review the court of appeals' extraordinary failure to decide the issues in the appeal duly pending before it, and its remand to the district court for the sole purpose of enabling that court to compound its error by (i) rescinding its prior order refusing to set aside the final judgment under Rule 60(b) as to co-defendant Abish, and (ii) vacating the final judgment as to Abish; both of which the district court promptly did.

(4) To review the refusal of the court of appeals to review, by appeal or by mandamus, the district court's coupling of its vacature of the final judgment with leave for Mahoney, Cohen (and subsequently Abish) to plead, and try to a jury, the defenses of

(a) lack of subject matter jurisdiction (alleged absence of the 28 U.S.C. §1332(a) $10,000 jurisdictional amount), and expiration of the statute of limitations, notwithstanding

(i) the express provisions of 28 U.S.C. §1332(b), which merely deny (or impose) costs in the event that a diversity plaintiff is ultimately adjudged to be entitled to recover less than $10,000 on his claim;

(ii) the district court's award of $35,803.75 in compensatory damages, exclusive of interest and costs, and $150,000.00 in exemplary damages;

(iii) the district court's ruling that "there [was] a good faith claim made when the lawsuit was filed in excess of ten thousand dollars" (A-54); and

(iv) the district court's ruling that "the issue of statute of limitations raised here is also without merit" (A-51).

(b) the alleged deposit to petitioner's account in 1980 of a $6,000 check dated in 1981, which alleged event the defendant accountants did not record on the books of

petitioner's former firm, but instead concealed in their private workpapers, and which they did not reveal despite repeated pre-suit inquiries by petitioner and the CPA he retained, notwithstanding their professional and fiduciary obligations to do so; and which alleged event does not qualify as newly discovered evidence under subdivision (2) of Rule 60(b), or excusable neglect under subdivision (1).

THE PARTIES

All parties are named in the caption. Mahoney, Cohen is a large Manhattan firm of CPA's practicing as a professional service corporation, which served petitioner's former law firm for many years prior to winding up its affairs. Abish was at all times here material an officer, director, shareholder and the corporate secretary of Mahoney, Cohen.

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REPORTED OPINION

The only reported opinion is Judge Brieant's May 13, 1987 Memorandum and Order adopting the Magistrate's Report as modified. *Vogt v. Abish, et al.*, 663 F.Supp. 321 (S.D.N.Y. 1987). The circuit's remand is noted at 842 F.2d 1288.

JURISDICTIONAL STATEMENT

The orders of the court of appeals remanding the case to the district court and denying the mandamus petition were filed May 12, 1988. No application or order respecting rehearing has been made, and the time for filing this petition has not been extended. The Court has jurisdiction to grant the writ pursuant to 28 U.S.C. §1254(1).

TEXT OF STATUTE AND RULES

STATUTE

28 U.S.C. §1332. **Diversity of citizenship; amount in controversy; costs**

(a) The district courts shall have original jurisdiction of all civil actions where the matter in controversy exceeds the sum or value of $10,000, exclusive of interest and costs, and is between—

(1) citizens of different States; ***

(b) Except where express provision therefor is otherwise made in a statute of the United States, where the plaintiff who files the case originally in the Federal courts is finally adjudged to be entitled to recover less than the sum or value of $10,000, computed without regard to any setoff or counterclaim to which the defendant may be adjudged to be entitled, and exclusive of interest and costs, the district court may deny costs to the plaintiff and, in addition, may impose costs on the plaintiff.

(c) For purposes of this section and section 1441 of this title, a corporation shall be deemed a citizen of any State by which it has been incorporated and of the State where it has its principal place of business: ***

***

FEDERAL RULES OF CIVIL PROCEDURE

Rule 54. **Judgments; Costs**

***

(b) **Judgment Upon Multiple Claims or Involving Multiple Parties.** When more than one claim for relief is presented in an action, whether as a claim, counterclaim, cross-claim, or third-party claim, or when multiple parties are involved, the court may direct the entry of a final judgment as to one or more but fewer than all of the claims or parties only upon an express determination that there is no just reason for delay and upon an express direction for the entry of judgment. In the absence of such determination and direction, any order or other form of decision, however designated, which adjudicates fewer than all the claims or the rights and liabilities of fewer than all the parties shall not terminate the action as to any of the claims or parties, and the order or other form of decision is subject to revision at any time before the entry of judgment adjudicating all the claims and the rights and liabilities of all the parties.

***

Rule 55. **Default**

***

(c) **Setting Aside Default.** For good cause shown the court may set aside an entry of default and, if a judgment by default has been entered, may likewise set it aside in accordance with Rule 60(b).

Rule 60. **Relief From Judgment or Order**

***

(b) **Mistakes; Inadvertence; Excusable Neglect; Newly Discovered Evidence; Fraud, etc.** On motion and upon such terms as are just, the court may relieve a party or a party's legal representative from a final judgment, order, or proceeding for the following reasons: (1) mistake, inadvertence, surprise, or

excusable neglect; (2) newly discovered evidence which by due diligence could not have been discovered in time to move for a new trial under Rule 59(b); (3) fraud (whether heretofore denominated intrinsic or extrinsic), misrepresentation, or other misconduct of an adverse party; (4) the judgment is void; (5) the judgment has been satisfied, released, or discharged, or a prior judgment upon which it is based has been reversed or otherwise vacated, or it is no longer equitable that the judgment should have prospective application; or (6) any other reason justifying relief from the operation of the judgment. The motion shall be made within a reasonable time, and for reasons (1), (2), and (3) not more than one year after the judgment, order or proceeding was entered or taken. A motion under this subdivision (b) does not affect the finality of a judgment or suspend its operation. This rule does not limit the power of a court to entertain an independent action to relieve a party from a judgment, order, or proceeding, or to grant relief to a defendant not actually personally notified as provided in Title 28, U.S.C., §1655 [relating to claims to or incumbrance of real or personal property], or to set aside a judgment for fraud upon the court. Writs of coram nobis, coram vobis, audita querela, and bills of review and bills in the nature of a bill of review, are abolished, and the procedure for obtaining any relief from a judgment shall be by motion as prescribed in these rules or by an independent action.

STATEMENT OF THE CASE

The district court had jurisdiction of this diversity action under 28 U.S.C. §1332(a). Petitioner is a citizen of Connecticut; Abish is a citizen of New York; Mahoney Cohen is a New York professional service corporation having its principal place of business in Manhattan.

PRE-SUIT EVENTS

Petitioner is a patent lawyer who practiced for many years as a partner in a Manhattan law firm (the "Watson" firm), which ceased operations as of April 30, 1981. Mahoney, Cohen ("MCC"), a firm of Certified Public Accountants which had rendered accounting services to the law firm for several years (preparing its financial statements and tax returns, *inter alia*), undertook to attend to winding up its non-legal affairs. MCC took custody of the firm's books and records, sold its assets, kept its books of account, made periodic distributions to the partners, prepared its 1981 financial statements, filed final 1981 tax returns in April 1982 and furnished to the Watson partners their Schedules K-1 (attachments to the federal partnership information return, Form 1065) setting forth their respective shares of partnership items. MCC thus served in both a professional and fiduciary capacity, and had corresponding obligations, as well as a contractual obligation, to the law firm and its partners. MCC was paid in excess of $78,000 for its services in winding up the Watson firm's affairs.

Abish, a CPA, had serviced the Watson account while with a prior accounting firm, and carried the account with him when he joined MCC in 1977 as an officer (the corporate secretary), director and shareholder. Abish continued to be principally responsible for servicing the Watson account at MCC. He signed all of the distribution checks drawn on the Watson bank account and received by petitioner subsequent to April 30, 1981.

The winding-up agreement between Watson and MCC provided for distributions to be made to the partners according to their cash capital balances. Expert testimony at the hearing before the Magistrate established that to be the only acceptable method for making liquidating distributions to partners. Petitioner was accordingly surprised to learn from the 1981 financial statements MCC prepared and distributed in the spring of 1982 that the distributions MCC made in 1981 were not proportionate. A May 1982 MCC memorandum to the Watson partners, signed by Abish, confirmed that the agreed procedure

had not been followed, and stated that as a result, some partners had been "overpaid," while others had been "underpaid."

According to MCC's 1981 Watson books, petitioner was one of the "overpaid" partners. The 1981 Schedule K-1 furnished to him reported that he had received in 1981 a disproportionate distribution under 26 U.S.C. §751 of $4,873, taxable as ordinary income. Petitioner accordingly included that item in gross income on his 1981 federal income tax return filed in mid-April 1982.

Evidence obtained by discovery in this action established that MCC was aware no later than April 2, 1982—almost two weeks before petitioner filed his return—that it had committed a negligent error in posting to petitioner's drawing account a $20,000 distribution made to another partner. It is also established that correction of that error converts the reported $4,873 of taxable ordinary income into a deductible $15,127 capital loss. Yet despite MCC's knowledge of its error, and that petitioner would perforce rely on the Schedule K-1 MCC had furnished to him, MCC did not inform petitioner of the error, or suggest that he obtain an extension. In order to correct the error, an amended partnership return appending revised Schedules K-1 would have to have been filed, and the correction would have affected the figures reportable by each of the partners. MCC made no effort to contact petitioner or otherwise inform him of the error. Instead, MCC actively concealed its error, in violation of its contractual, professional and fiduciary obligations, and knowingly suffered petitioner to report income he did not in fact receive and pay income taxes he did not owe. That egregious misconduct is one basis for the award of exemplary damages to petitioner.

Petitioner had always accepted the financial statements prepared by the MCC CPA's without question. But being greatly disturbed by the non-proportionate distributions reported in the 1981 financial statements and the May 1982 MCC memorandum, petitioner was moved to add up the Watson distributions he had received in 1981. His total was some

$26,000 less than the figure reflected on the MCC financial statements. At that point petitioner retained a CPA, Paul M. Koren of a Manhattan public accounting firm, to look into the matter on his behalf.

In June 1982 Koren went to the MCC offices, where the Watson books were kept, and readily found the $20,000 posting error. The other component of the shortfall was a $6,000 distribution check posted to petitioner's drawing account and recorded in the Watson cash disbursements journal (check register) in January 1981. Petitioner had no record of receiving a $6,000 check in January 1981, and MCC could provide no explanation, either at that time or on the numerous other occasions when petitioner and/or Koren made inquiry concerning it. Koren at once requested copies of all cancelled 1981 checks payable to petitioner; MCC provided them in late 1982, but there was no January 1981 check, and MCC could provide no explanation for its absence.

At a January 1983 meeting at the MCC offices attended by petitioner, Koren, Abish and other MCC personnel, MCC freely admitted the $20,000 posting error and promised to file an amended partnership return with revised Schedules K-1 so that petitioner could apply for refund of the excessive taxes he had paid by reason of MCC's error. There was still no cancelled check and no explanation for the $6,000 item, and MCC promised to make one more attempt to resolve that item. Months dragged by without any remedial action by MCC. Abish did not answer Koren's telephone calls.

THE IRS EXAMINATION

In October 1983 the IRS examined the 1981 Watson partnership return at the MCC offices. Abish had confirmed to Koren and petitioner at the January 1983 meeting that the correction of the $20,000 posting error would affect each of the 13 Watson partners' Schedules K-1 (hence their respective reportable incomes, hence their respective tax liabilities). It is evident that MCC did not reveal its posting error, and the consequent inaccuracy of the Watson partners' Schedules K-1,

to the IRS examiner; IRS informed petitioner in writing on March 25, 1985: "We have no record of ever receiving an amended [partnership] return. There was no tax liability on the original return filed, and there were no changes made as the result of the examination." Thus, MCC's coverup of its error even extended to active concealment from the IRS.

THE FINAL EFFORT TO AVOID SUIT

In one last effort to avoid litigation following a protracted period of inaction by MCC, petitioner asked Koren to arrange a top-level contact between his firm and MCC. In late 1984 Gerald Golub, the Managing Partner of Koren's firm, telephoned Arnold Cohen, the Managing Partner of MCC. Mr. Golub has sworn:

> I made the call to Mr. Cohen, whom I have known for many years, both because Mr. Koren suggested that I do so on Mr. Vogt's behalf, and also as a courtesy to Mr. Cohen. Mr. Cohen thanked me for the call, and I did not hear further from him concerning the matter.

The complaint was filed January 3, 1985.

THE SUIT

The complaint alleges breaches of contract, malpractice and negligence, breaches of professional and fiduciary duties and fraud, and seeks compensatory and exemplary damages. The defendants were separately served by certified mail pursuant to F.R.Civ.P. 4(c)(2)(C)(ii). The postal return cards were signed by Rose Hirschberg, the MCC receptionist. In February two letters concerning the suit were sent to defendants by certified mail; the postal return cards were again signed by Ms. Hirschberg.

When neither defendant returned the acknowledgment form enclosed with the complaint (which the district court clerk had provided), follow-up personal service was made pursuant to Rule 4 by personal delivery of two copies of the summons and complaint to Abish, by appointment. No response was

thereafter made, and defendants' default was noted on April 10, 1985. The matter was referred to the Magistrate for supervision of discovery and recommendation of damages.

POST-SUIT EVENTS

The Magistrate's June 1985 order to produce documents was served by certified mail separately addressed to Abish and "Managing Partner, Mahoney, Cohen & Co., P.C." Ms. Hirschberg again signed both postal return cards. Uncertified letters were sent to defendants on July 31 and October 31, 1985.

Meanwhile, on February 6, 1985, about a month after suit was filed, petitioner received from MCC by express mail an "Amended" Schedule K-1, together with Abish's note identifying it as such. The "Amended" K-1 differed from the original K-1 by substituting a *deductible* $15,127 capital loss for the previously reported *taxable* $4,873 of §751 ordinary income. The new K-1 had every appearance of being genuine, and as it came from a firm of certified public accountants and was accompanied by a note stating that it was what it appeared to be, petitioner believed he could properly rely on it; he did, however, request confirmation that the amended partnership return had in fact been filed. That letter was also sent by certified mail (signed for by Rose Hirschberg) the same day the "Amended" K-1 was received. A month went by before petitioner received the stonewalling reply that MCC was "putting together the information you requested and will have same sent to you no later than March 20, 1985." There was no further reply to petitioner's simple question by that date, or at any later time.

Being aware that the three-year period within which to file an amended 1981 personal income tax return would expire April 15, 1985, petitioner took it upon himself to correspond directly with IRS. On March 29, 1985 petitioner received the IRS response quoted *ante*, p. 7. The "Amended" K-1 was thus a sham, designed to deceive both petitioner and the court.

In mid-1986 Abish proposed that petitioner stay the suit in return for a $5,000 "good faith" payment to be credited against a sum which Abish promised to calculate at some indefinite date. The suit would not have been filed but for repeated broken promises, and petitioner declined the proposal. Documents were slowly produced following service of the discovery order (Abish pleaded absence for jury duty), and in January affidavits and exhibits were filed to quantify the claimed compensatory damages and support the request for exemplary damages. The Magistrate held a trial at which petitioner, Koren and Professor Joseph C. DiBenedetto, a lawyer, CPA and former chair of the Pace University accounting department testified.

Chief Judge Brieant's Chambers sent the Magistrate's report (A-4, 64) to each defendant on March 27, 1987. The letters were received, and are even annexed to MCC's Rule 60 affidavits. MCC nevertheless insisted that it never received notice of the action prior to entry of judgment. Neither MCC nor Abish responded to the court's letters.

Petitioner's limited exceptions to the Magistrate's report were in part sustained. The Magistrate recommended both compensatory and punitive damages. Petitioner advanced two bases in support of his claim to punitive damages: (1) defendants' knowingly improper exclusion of him from the May 1982 distribution (which was subsequent to their April 2 knowledge of their $20,000 posting error), and (2) defendants' failure to file an amended partnership return with corrected Schedules K-1, as they had repeatedly represented and promised they would do. The Magistrate sustained the second of those grounds, but rejected the first, on the theory that knowledge of the $20,000 posting error by April 2, 1982 could not be imputed to MCC. Judge Brieant differed with the Magistrate and sustained both grounds, but did not enlarge the punitive award (A-41-42). The $6,000 item was never part of the request for, or the award of, punitive damages.

THE POST-JUDGMENT PROCEEDINGS

Judgment was entered concurrently with Judge Brieant's memorandum and order on May 14, 1987. Petitioner moved to amend the judgment on the ground that the court had misapplied New York law in *sua sponte* disallowing the excessive 1981 income taxes as an element of compensatory damages, and tendered Mr. Koren's affidavit to show that the court's newly postulated proposal that either petitioner or Koren should have filed an amended partnership return was neither realistic nor feasible, and that Koren's firm would not have accepted the engagement. The motion was summarily denied on July 14 without opinion. Petitioner duly noticed an appeal from that ruling.

On May 28, 1987 MCC procured the resignation of Abish, its corporate secretary and director, and on June 9 applied by order to show cause to have the judgment against it set aside under Rule 60(b)(4) and (6) for "lack of subject matter jurisdiction and lack of personal jurisdiction, and in the interests of justice." MCC sought to paint Abish, its long-time officer and director, as an adverse agent, and advanced the theory that unless Mr. Mahoney or Mr. Cohen—each of whom owned 33% of the corporate stock—had personally been informed of the suit, the corporation did not have notice of it. It was admitted that an investigation of the corporate files revealed that the summons and complaint had indeed been served on MCC.

Chief Judge Brieant found the assertion of lack of jurisdiction to be without merit (A-51). He also reaffirmed the propriety of the award of punitive damages, pointing out that MCC had actual notice of the $20,000 posting error through Mr. Koren's discovery of it in the presence of MCC accountant Bruce Chew, as well as through Abish and "N.S.", the author of the April 2, 1982 document recognizing the posting error (A-53). Judge Brieant added:

> So, the Court concludes there was adequate basis for the punitive damages award. And there is a public interest in this type of performance and lack of familiarity and lack of

> proper supervision, if that is what occurred here, at least as serious as MCC's failure to insure that [a] lawsuit filed against it will come to the attention of the majority stockholders. [A-53]

Purporting to act under Rule 60(b)(6), Judge Brieant nevertheless granted MCC's application, solely on the ground that MCC "may have a partial meritorious defense" to the $6,000 claim (A-54, 57). Petitioner noticed an appeal from that ruling, believing that the district court had disregarded controlling precedents and ignored the severe prejudice to petitioner resulting from passage of time since the events of 1980—the dispersal of the actors, MCC's admitted loss of the $6,000 check on which its alleged defense depends, Abish's newly professed alcoholism and his servient posture vis-à-vis MCC, which now holds his $282,000 interest in that firm.

The "partial meritorious defense" on which the district court's ruling hinges was not mentioned in MCC's moving papers. It was first advanced in an affidavit of Rehmet, a vice president who joined MCC in 1983, well after the events concerning which he undertook to testify. Rehmet relied on an internal MCC workpaper relating to preparation of the 1980 Watson financial statements—which was not distributed to the Watson partners—to postulate that a group of partner draw checks dated in January 1981 were deposited in and cleared by Chemical Bank at the end of December 1980. One of the checks is said to have been payable to petitioner. MCC cannot produce the cancelled check, however, and the Chemical Bank microfilms from that period have been destroyed.

Thus, five years after the June 1982 meeting at which Koren first requested the cancelled check or an explanation, neither of which MCC was able to provide, then or later, MCC castigated both petitioner and Koren for not having at once assumed that the missing check had been deposited and had cleared in the prior year—even though it was posted to petitioner's account, and entered in the cash disbursements journal, in January 1981, not December 1980; and even though that possibility never occurred to the MCC accountants, in

whose private workpapers that explanation is said to have been hidden all those intervening years.

The theory which so long eluded MCC has now become the sole basis for the district court's excusing MCC's default and its failure to respond to service of process and to the Magistrate's report which Judge Brieant sent to MCC. That alone is the supposed justification for setting aside the judgment, purportedly under Rule 60(b). The courts below took no account of MCC's fiduciary duty to reveal the hidden information to petitioner and his accountant when asked, or their clear professional obligation to do so.[1]

Although the ruling setting aside the judgment as to MCC quite ignores the prejudice to petitioner resulting from the passage of time (MCC's loss of the cancelled check and Chemical Bank's destruction of the microfilm), that prejudice was taken into account by the district court and included as a compelling reason for refusing to set aside the judgment as to Abish (A-63). In the court of appeals all counsel agreed that the two rulings could not be reconciled, and the appellate court made certain inquiries of Judge Brieant (A-70). The response (A-73) quotes those inquiries, but does not respond directly to them; it instead urges that the court of appeals deny the mandamus petition and remand so that the district court could set aside the judgment as to Abish, as well (A-77).

The court of appeals acceded to that request (A-1, 2), without opinion and without deciding any of the issues before it. Symmetry was thereby achieved at the price of justice.

[1] ET § 501.02 of the American Institute of Certified Public Accountants Professional Standards is directly in point. It provides:

> A member's working papers are his property and need not be surrendered to the client. However, in some instances a member's working papers will contain data which should properly be reflected in the client's books and records but which for convenience have not been duplicated therein, with the result that the client's records are incomplete. In such instances, the portion of the working papers containing such data constitutes part of the client's records, and copies should be made available to the client upon request.

There was no serious effort by either defendant to show that the ruling as to Abish was legally erroneous; only that it was inconsistent with the ruling as to MCC. But two wrongs do not make a right, and neither court below has written one word to suggest that the Rule 60(b) analysis as to Abish's application was in error, or to justify reversing it. *Sub silentio,* it is another illustration of the legally erroneous view, expressed in the ruling as to MCC, that the district court has unfettered license to do as it pleases under the "grand reservoir" allegedly provided by subdivision (6) of the rule.

According to MCC's new theory, the $6,000 draw was deducted from the Watson bank account in 1980. In order for the books to balance, the draw would likewise have to have been charged to petitioner's account in 1980, rather than in 1981. The 1980 MCC workpapers, which were reviewed and approved by Abish in January 1981, indicate that MCC adjusted the Watson books, without the Watson partners' knowledge, to make it appear that the draw checks now alleged to have been paid in December 1980 were instead paid in 1981. The 12/31/80 bank balance was adjusted (reconciled), first by the usual step of deducting outstanding checks, and then by the unusual step of adding back "Jan. checks cleared in Dec.", thereby arriving at an adjusted bank balance which was carried forward to the 1980 trial balance and the 1981 opening bank balance.

MCC's alterations thus made it appear from the Watson books that the checks had been paid in 1981, rather than in 1980. That bit of accounting legerdemain is revealed only by MCC's internal workpapers; it cannot be divined from the Watson books. There is no notation on the 1981 Watson check register (journal) which Koren and the MCC accountants examined in June 1982 to show the very different state of facts MCC now postulates. Quite evidently, no one at MCC thought to look for a cancelled 1981 check in the December 1980 bank statement; the Watson books indicated it would be enclosed with the January 1981 statement.

MCC was thus hoist by its own petard. Only MCC had knowledge of the adjustment; Koren and petitioner had no way of knowing or divining that it lay buried in the internal workpapers Abish had signed and approved. Petitioner did not succeed in getting that point across to the district court, however:

> MR. VOGT: ... Secondly, Mahoney, Cohen has a lot to do with it. If it were not for their 1980 workpapers that would have been charged as a 1980 draw.
>
> THE COURT: I don't agree with that. There is no use belaboring it. It is wrong for a check to be deposited before its date.

It had long been the practice that the Watson bookkeeping department deposited petitioner's draw checks, as the endorsements (or lack thereof) on the copies of the 1981 Watson checks furnished by MCC to Koren in late 1982 and submitted with petitioner's affidavit confirm. The quoted colloquy shows that the alleged anomaly on which the district court based its Rule 60(b) order would no more have occurred to the district court than it did to the MCC CPA's, to CPA Koren and to petitioner.

Judge Brieant concluded that petitioner believed, and had pleaded in good faith, that he had not received the January check. The court was "not convinced that a total search of an adequate nature has been made [for] these records which are in the possession of Mahoney, Cohen" (A-55). The court added:

> If you actually had the check with his endorsement [on] it, then there would be no room for any dispute. ... I think viewed most favorably to Mahoney, Cohen, it is a jury question whether he got it.

That, however, is not the question under Rule 60(b). Both MCC and the court relied on allegedly newly discovered

evidence. But that is not enough; subdivision (2) of the rule applies only when there is

> newly discovered evidence which by due diligence could not have been discovered in time to move for a new trial under Rule 59(b).

The Rehmet affidavit setting forth the alleged new evidence is sworn only a week after MCC's Rule 60(b) application was filed. The alacrity with which the workpaper story was developed illumines a striking absence of diligence on the part of MCC, dating from 1982.

Following entry of the July 17 Order setting aside the judgment as to MCC, Abish promptly appeared by counsel and sought like relief. His story (not pressed on appeal) was that he had entered an institution the week before to be treated for chronic alcoholism. His counsel's me-too argument, however, was that "Abish has got the same meritorious defense that Mahoney, Cohen has and your Honor has already adjudicated that". Judge Brieant analyzed the Rule 60(b) standard and denied Abish's application for want of any showing of legal incapacity, failure to establish that his default was not willful, laches and prejudice to petitioner

> "especially in as far as [during] the intervening period, the bank destroyed the microfilm of [the $6,000] check". [A-63]

REASONS FOR ALLOWANCE OF THE WRIT

Rule 60(b) embodies a fundamental principle of federal jurisprudence. Uniform application of the rule by the inferior courts is consequently a matter of signal importance. The Court has not addressed Rule 60(b) of late; we respectfully submit that the tangled morass below eloquently establishes the need for the Court to do so.

This case truly provides a textbook illustration of the wisdom of the standards for setting aside a judgment spelled

out in the rule and the decisions construing it. But it also demonstrates the chaos that results when the rule and its implementing decisions are not heeded, and individual judicial notions of the content of a "grand reservoir" are interjected willy nilly. There remains a reservoir of confusion and uncertainty in the lower courts:

> Thus whether the water in the reservoir is scant or grand, is far from clear.

Nemaizer v. Baker, 793 F.2d 58, 63 (2d Cir. 1986). Only the Court can provide that much-needed clarification.

The aggravated situation created in the district court was materially exacerbated by the circuit's unexplained departure from its long line of holdings that Rule 60(b) issues are to be addressed by appeal, rather than mandamus. According to Moore's treatise, relatively few circuits follow that procedure. 7 Moore's Federal Practice ¶60.30 [3]. The Second Circuit has taken note of the commentators' criticism, but has adhered to its practice as one impelled by this Court's decisions. *Rinieri v. News Syndicate Co., Inc.,* 385 F.2d 818, 821-22 (2d Cir. 1967). It would be beneficial to Bench and Bar were the Court to address that conflict among the circuits as well.

The circuit's professed concern with its jurisdiction, which came as a surprise to all counsel (none had suggested it), is respectfully believed to be misplaced. To be sure, the incantation of the "no just reason for delay" phraseology of Rule 54(b) appears in transcript (A-64), rather than in Judge Brieant's implementing endorsement (A-68). The transcript also contains the district court's explanation ("reasoned statement") for its action. The circuit's jurisdictional concern seems quite evidently to have overlooked the 1961 amendment of Rule 54 to include within its ambit jointly liable parties. The Advisory Committee note points out that the amendment did away with the problem of appealability upon entry of judgment as to less than all the jointly liable defendants. As Moore observes, "it is no longer necessary to determine whether the claim against a party is joint or several, or separate and distinct." 6 Moore's Federal Practice ¶54.04 [3.-8], at 54-56.

Above all, we respectfully submit, the proceedings in both courts below point up the need for the Court to revisit and reiterate its 38-year-old admonition in *Ackermann v. United States,* 340 U.S. 193, 199 (1950), that the "any other reason justifying relief" language of subdivision (6) is not a lock which virtually any key will fit; and that truly "extraordinary circumstances" are very much a prerequisite to its invocation.

There is abundant language in the opinions of the circuit below which accord with *Ackermann.* "Since 60(b) allows extraordinary judicial relief, it is invoked only upon a showing of exceptional circumstances." *Nemaizer v. Baker, supra,* 793 F.2d at 61. The words are fine, but it is the action that counts. Exercise of the Court's supervisory authority over the regional circuits to require compliance with established principle provides a further compelling reason for allowing the writ. A messy situation in the district court should not be met by silence and abdication of appellate responsibility.

The absence of any guidance from the circuit accompanying its remand in response to the district court's announced intention to withdraw its correct application of Rule 60(b) as to Abish in favor of unlawful symmetry should not, we respectfully submit, be brushed aside unnoticed by the Court. Although this is not a court of error, supervisory authority carries with it the need to single out and nip in the bud practices which can only grow if winked at.

The circuit has also recognized that the legal standard for relieving a defaulting party from the judgment under Rule 60(b) is far more stringent than the relatively lenient test for vacating a default prior to entry of judgment under Rule 55(c). *E.g., Davis v. Musler,* 713 F.2d 907, 915 (2d Cir. 1983). The Rule 55(c) test is three-pronged: whether the default was willful, whether setting aside the default would prejudice the adversary, and whether a meritorious defense has been presented. *Meehan* v. *Snow,* 652 F.2d 274, 277 (2d Cir. 1981). Even under that liberal test it was error for the district court to focus

only on its presumption of the merit of the proposed defense. That error clearly appears from the district court's explanation:

> The Court would deny the [MCC] motion brought by the Order to Show Cause in all respects, but for one thing and that is that the Court has concluded that Mahoney, Cohen and Company has established on this motion a meritorious partial defense which it should have the right to have considered and tried to the Court. Where a party establishes a meritorious defense to a claim adjudicated on default, and there is no significant prejudice to the other side of the case, our court liberally construes Rule 60(b) motions to promote the resolution of lawsuits on the merits rather than by default.
>
> The Court relies on Radack in the Second Circuit in 1963 [*Radack* v. *Norwegian America Line Agency, Inc.*, 318 F.2d 538 (2d Cir. 1963)], which quote a grand reservoir of equitable power to do justice is said to be available in determining whether to vacate a judgment. And the Court has consistently held this rule should be construed freely when substantial justice will be served. [A-54]

The *ratio decidendi* is thus but one prong of the Meehan test for vacating a default *prior* to judgment under Rule 55(c), in contrast to the far more stringent "exceptional circumstances" test applicable to motions under Rule 60(b). The supposed meritorious partial defense upon which Judge Brieant focused is not enough. "The movant must of course establish that his cause has merit, but he must further come within the statutory scheme of Rule 60(b)." *United States* v. *Cirami*, 535 F.2d 736, 742 (2d Cir. 1976). Moreover, the liberal construction to which Judge Brieant referred "is usually reserved for instances where error is due to the failure of attorneys or other agents to act on behalf of their clients, not where the client's own internal procedures are at fault." *Greenspun* v. *Bogan*, 492 F.2d 375, 382 (1st Cir. 1974)(citing *Supermarkets General Corp.* v. *Grinnell Corp.*, 59 F.R.D. 512, 514 (S.D.N.Y. 1973)).

The story of the $6,000 check which MCC now advances should have been made known to Koren and petitioner in June 1982. That it was instead concealed does not excuse the inadequacy of MCC's internal office procedures to make Messrs. Mahoney and Cohen personally aware of service of process and certified mail concerning the suit—including the certified mail addressed to the Managing Partner of MCC. And it is clearly MCC's own internal procedures (or lack thereof) which are at fault. Majority shareholders who so distance themselves from knowledge of service of process can hardly expect judicial sympathy for their failure to establish proper controls. As another district court well put it in *International Corporate Enterprises, Inc.* v. *Toshoku Ltd.*, 71 F.R.D. 215, 217-18 (N.D. Tex. 1976):

> The Court is of the opinion that the facts of this case show gross carelessness on the part of defendant, rather than excusable neglect, mistake or inadvertence. If a foreign corporation does business in Texas by entering into contracts with corporations of Texas, to be performed in whole or in part here, it must take steps to insure that its internal procedures allow it to be responsive to legal proceedings in this state. Failure of Toshoku's internal structure to provide a mechanism for response is not excusable neglect. [Citing *Supermarkets General* and *Greenspun, supra*]

Perforce, those observations apply with even greater force to a domestic corporation, such as MCC.

The matter of substantial prejudice to the plaintiff, stressed in the district court's first ruling as to Abish (A-63), and thereafter ignored by it and the court of appeals, takes the case outside the lenient good cause test of Rule 55(b). *Cf. Original Appalachian Artworks, Inc.* v. *Yuil International Trading Corp.*, 105 F.R.D. 113, 118 (S.D.N.Y. 1985)(prejudice found as a matter of law where vacature of default was sought after Magistrate had held damages inquest). The Rule 55(c) test is not met at bar for the further reason that MCC failed to show a

valid excuse for its default. *Cf. Taylor* v. *Boston and Taunton Transp. Co.*, 720 F.2d 731, 733 (1st Cir. 1983). *A fortiori* the more demanding Rule 60(b) standard is not satisfied. Judge Brieant correctly held that Abish's actions and knowledge must be imputed to MCC; *see Szajna* v. *Rand,* 75 A.D.2d 617, 427 N.Y.S.2d 57 (2d Dept. 1980).

Moreover, as service of process was validly effected both by mail and by follow-up personal service, the ruling below eviscerates Rule 4 and stands as a dangerous precedent to be taken advantage of by those who would await the outcome and only then appear and contest the result, if it be unduly unfavorable. That danger is not ameliorated by alluding to Professor Moore's aphorism, "grand reservoir of equitable power to do justice." As applied below, the aphorism became a shibboleth which impermissibly ignored the *Nemaizer* admonition, *supra,* that "[t]his portion of the Rule is properly invoked only when there are extraordinary circumstances justifying relief" (citing *Matter of Emergency Beacon Corp.,* 666 F.2d 754, 759 (2d Cir. 1981)). 793 F.2d at 62. There are no extraordinary circumstances warranting vacature here; MCC complains only of a self-inflicted wound.

As was clearly pointed out in *Rinieri, supra,* 385 F.2d 818 at 822,

> if [the district court] acted without any basis in law, disregarding the limitations placed upon the power to vacate provided in the provisions of Rule 60(b), [it] lacked jurisdiction to act and this order is *appealable.* [Emphasis added]

A more direct and explicit holding cannot be imagined. Yet the circuit simply chose to ignore that controlling precedent, which was squarely brought to its attention, both in response to MCC's motion to dismiss and in the petition for rehearing *in banc.* The Court in its supervisory role should, we submit, take note of the harsh penalty inflicted on petitioner for a sin no more grievous than following a procedure the circuit's decisions have mandated.

Petitioner thereupon resorted to application for the extraordinary writ of mandamus. Footnote 10 of the *Rinieri* opinion observes, "[t]he normal remedy for action taken in

excess of jurisdiction is mandamus [citing *International Products Corp.* v. *Koons,* 325 F.2d 403, 407 (2d Cir. 1963)]." Yet the mandamus petition was denied without any indication of reason, after the district court had characterized it as an impediment to reversing the initial ruling on the Abish application (A-77).

Even though the $6,000 check was found to be MCC's only "partial meritorious defense," the district court did not limit the reopening to that one item. All of the Magistrate's work underlying his lengthy comprehensive report (A-4-31) was thereby discarded, and the same ground will have to be replowed at trial by the court and a jury, notwithstanding the ruling that MCC has no other meritorious defenses. Time spent recanvassing that ground cannot be devoted to other pressing matters.

At the July 31, 1987 Abish hearing the district court made clear that it regarded MCC's partial defense as tenuous, and stated that it "reluctantly" granted the Rule 60(b) application because MCC "came close to presenting what might be a valid partial defense" (A-63-64). That, of course, is a far cry from the "extraordinary circumstances" required by this Court in *Ackermann,* and by the Second Circuit in *Nemaizer, supra.*

The district court received no further evidence before making its April 1988 response to the court of appeals. There is accordingly no new factual basis to support the castigating of petitioner (A-76-77) for "unreasonable refusal" to admit receipt of the check and failure to file an amended partnership return (a matter which the appellate court has thus far refused to review). Moreover, the request for, and award of, punitive damages had nothing to do with the $6,000 check, as the district court's May 1987 memorandum makes plain (A-41).

Chief Judge Brieant is surely correct that the current "procedural morass" is offensive to the F.R.Civ.P. Rule 1 goal that the rules "be construed to secure the just, speedy and inexpensive determination of every action" (A-76). None of those wholesome objectives has been achieved here. This

grossly aggravated situation can only worsen unless the Court exercises its supervisory authority to bridle it.

This simple matter, involving unmistakable wrongdoing by licensed professionals who have yet to utter one word of apology for their litany of misdeeds, and who insist that accountants constitute a privileged class against whom punitive damages cannot be awarded, has grown to become a monster. It is too late to nip this case in the bud, but it is not too late to avoid further waste of precious judicial resources at the trial and appellate levels on a matter which should have found repose well before the end of 1987.

A fresh elucidation of the Rule 60(b) standard, and particularly the standard applicable to subdivision (6), would spare untold hours of judicial labor and truly foster the just, speedy and inexpensive determination of actions governed or affected by the rule.

CONCLUSION

For the reasons stated, the writ should be allowed.

Respectfully submitted,

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APPENDIX

[Filed May 12, 1988]

United States Court of Appeals

FOR THE

SECOND CIRCUIT

At a stated Term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse in the City of New York, on the 12th day of May, one thousand nine hundred and eighty-eight.

Present:

HONORABLE WILFRED FEINBERG, *Chief Judge*

HONORABLE WILLIAM H. TIMBERS,

HONORABLE AMALYA L. KEARSE, *Circuit Judges*

WILLIAM H. VOGT, III,

Plaintiff-Appellee, Cross-Appellant,

—against—

SHELDON ABISH and MAHONEY, COHEN & CO., P.C.,

Defendants-Appellants,

MAHONEY, COHEN & CO., P.C.,

Defendant-Appellant, Cross-Appellee.

87-7688
87-7738
87-7718

An order of this court was entered on February 4, 1988, remanding the case to the district court for clarification of certain matters concerning our jurisdiction to hear the arguments raised on the appeals and cross-appeal. On April 19,

1988, Chief Judge Brieant filed a Memorandum and Order in response to our order, which has been filed with this court and commented on by the parties. In view of the matters set forth in that Memorandum and Order, we hereby remand the entire case to the district court for such further proceedings as the district court deems appropriate.

WILFRED FEINBERG

Wilfred Feinberg, Chief Judge

WILLIAM H. TIMBERS

William H. Timbers,

AMALYA L. KEARSE

Amalya L. Kearse,
Circuit Judges.

A True Copy
ELAINE B. GOLDSMITH

ELAINE B. GOLDSMITH

Clerk

This summary order will not be published in the Federal Reporter and should not be cited or otherwise relied upon in unrelated cases before this or any other court.

[Filed May 12, 1988]

United States Court of Appeals

FOR THE

SECOND CIRCUIT

At a stated Term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse in the City of New York, on the 12th day of May, one thousand nine hundred and eighty-eight.

Present:

HONORABLE WILFRED FEINBERG, *Chief Judge*
HONORABLE WILLIAM H. TIMBERS,
HONORABLE AMALYA L. KEARSE, *Circuit Judges.*

In re WILLIAM H. VOGT III, *Petitioner.*	88-3004

A petition for writ of mandamus having been filed by William H. Vogt, III on January 21, 1988.

UPON CONSIDERATION THEREOF, it is ordered that the petition be and it hereby is denied.

WILFRED FEINBERG
Wilfred Feinberg, Chief Judge

WILLIAM H. TIMBERS
William H. Timbers

AMALYA L. KEARSE
Amalya L. Kearse, Circuit Judges.

A True Copy

ELAINE B. GOLDSMITH

by KATHLEEN BROWN
Deputy Clerk

[Filed March 27, 1987]

United States District Court
Southern District of New York

WILLIAM H. VOGT III,

Plaintiff,

—against—

SHELDON ABISH and
MAHONEY, COHEN & CO., P.C.,

Defendants.

Report and Recommendation

85 Civ. 0088 (CLB)

TO THE HONORABLE CHIEF JUDGE CHARLES L. BRIEANT, U.S.D.J.:

By Order dated June 13, 1985 (filed June 14, 1985), The Honorable Lee P. Gagliardi, D.J., to whom this case was initially assigned, referred the same to the undersigned for "supervision of any necessary discovery on the issue of damages, determination of any related motions, and report and recommendation on the amount of plaintiff's damages," in light of defendants' default in moving or answering with respect to the complaint. *See* Clerk's Certificate of Default, filed June 10, 1985. Subsequently, the case was reassigned to The Honorable Chief Judge Charles L. Brieant, who expressly continued the reference.

Documentation was first submitted by plaintiff for preliminary analysis, in part, to determine if a hearing was necessary, whereupon I determined that it was and a hearing was held on December 19, 1986, whereat plaintiff, William H. Vogt III, Esq. ("Vogt") (Tr. 7, *et seq.*),* his expert Certified Public Accountant, Paul M. Koren ("Koren") (Tr. 108, *et seq.*), and

* "Tr." refers to the transcript of the hearing, with the numbers following representing the page(s) thereof.

Professor of Accounting, Joseph C. DiBenedetto ("DiBenedetto") (Tr. 166-167, *et seq.*), testified and certain exhibits were then also introduced into evidence. The matter was fully submitted on January 13, 1987, upon my receipt of the hearing transcript and other supplementary materials made necessary by our prior inquiries.

Based on the evidence and reasonable inferences drawn therefrom, I respectfully submit my findings of fact, conclusions of law and recommendations.

BACKGROUND

Vogt, formerly a partner in Watson Leavenworth Kelton & Taggart, Esqs. ("WLKT"), a New York City law partnership which ceased operations at the close of business on April 30, 1981, brings this action against the firm's outside certified public accountants, Mahoney, Cohen & Co., P.C. ("MCC") and Sheldon Abish ("Abish"), a principal of MCC, for alleged improprieties during the course of WLKT's liquidation. Complaint, at ¶¶ 2, 3, 5-6. MCC had previously rendered accounting services to WLKT for several years prior to the firm's dissolution and was engaged to wind up the financial and non-legal business affairs of the partnership through an agreement entered into in March or early April 1981. Complaint, at ¶¶ 6-7; Letter to the Magistrate from Vogt, dated September 25, 1986, at 1-2 and Hearing Exhibits ("Ex.") 26-35.** The agreement obligated MCC, Vogt says, "to carry out their activities [relevant to dissolution of WLKT] in a businesslike, fair and accurate manner, without favor or disfavor towards plaintiff, and in accordance with sound and accepted accounting principles. Complaint, at ¶ 8; *see also*, Ex. 24. Abish was the MCC partner primarily responsible for handling the WLKT account and overseeing dissolution of the partnership. Complaint, at ¶ 6. Jurisdiction is properly grounded on diversity of citizenship. Complaint, at ¶¶ 1-4.

** Vogt introduced 56 exhibits at the hearing in support of his application for a default judgment.

In his Complaint, Vogt charges Abish and MCC with breach of contract (Counts I and II), professional malpractice and negligence (Count III), and breach of fiduciary duties and fraud (Count IV), all stemming from a $6,000 partnership distribution charged to Vogt's drawing account, but never received by him, and a $20,000 posting error, causing Vogt to receive less than his fair share of partnership distributions and, in turn, requiring him to pay excessive taxes on what he did receive. *See* Complaint, at ¶¶ 12-22; Vogt Affidavit, sworn January 21, 1986, at ¶¶ 5, 7-9 ("Vogt Aff.").[1] Vogt discovered MCC's errors after retaining Koren, a certified public accountant and a member of the New York City certified public accounting firm, Goldstein, Golub, Kessler & Co., P.C., when he was unable to reconcile MCC's figures with his records. Complaint, at ¶ 11; Vogt Aff., at ¶ 4. Vogt seeks as relief compensatory damages, accounting and legal fees and punitive damages.

At the root of this controversy are two serious accounting errors made during the course of WLKT's liquidation, which, unattended, have snowballed into a course of events resulting in Vogt incurring unnecessary financial loss. More specifically, MCC had charged a $6,000 distribution to Vogt's partnership drawing account for January 1981, which Vogt affirms he never received. Vogt Aff., at ¶ 7; Koren's Declaration, executed January 21, 1986, at ¶ 4 ("Koren Dec."); Ex. 11. Indeed,

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[1] As aforesaid, prior to the hearing, Vogt submitted, *inter alia*, his affidavit to the Court in support of his application for a default judgment. Subsequently, it was determined that a hearing was necessary in light of the Court's prediliction to grant Vogt punitive damages on the basis of the contents of Vogt's affidavit and a declaration by Koren, executed January 21, 1986 ("Koren Dec."). Punitive damages may not be awarded by a court in the absence of an evidentiary hearing where the court must assess "the degree of wanton and willful conduct of the defendant[s]." *Flaks v. Koegel*, 504 F.2d 702, 707 (2d Cir. 1974); *Deshmukh v. Cook*, 630 F.Supp. 956, 959-960 (S.D.N.Y. 1986). At the hearing Vogt and Koren expressly adopted the contents of their previously filed papers and subsequent discussion in text shall refer to Vogt and Koren's attestations, and relevant excerpts from the hearing transcript. (Tr. 99, 143-144).

Koren's examination of MCC's checks payable to Vogt for 1981 failed to disclose the $6,000, 1981 distribution check and Koren states, defendants "acknowledged that they did not have a cancelled check or other record to support the entry." Koren Dec., at ¶ 4; Tr. 115, 122, 126.

The second error disclosed by Koren's examination of MCC's accounting records was a $20,000 partnership distribution charged to Vogt's drawing ccount, which was paid not to Vogt, but rather to WLKT partner, Nick Stathis. Koren Dec., at ¶ 5; Vogt Aff., at ¶ 8; Exs. 11 and 16; Tr. 42, 116. MCC conceded the error to Koren in 1982 and to Vogt in January 1983. Koren Dec., at ¶ 5; Vogt Aff., at ¶¶ 8-9; Exs. 16 and 17; Tr. 48, 122-123, 126.

On account of the posting error, Abish had agreed, in a meeting with Vogt and Koren on January 24, 1983, to file an amended partnership return with accompanying amended Schedules K-1 to reflect the error, permitting Vogt to then file amended federal and state personal tax returns to obtain tax refunds. Vogt Aff., at ¶ 9; Koren Dec, at ¶ 5; Exs. 16 and 17; Tr. 50, 137.

As the result of the $20,000 posting error, MCC had initially reported to Vogt that he had to recognize $4,873 as §751 ordinary income (*see* 26 U.S.C. §751) for the 1981 tax year and realized no long-term capital losses incident to WLKT's dissolution. *See* Exs. 3, 48; Vogt Aff., at ¶ 8; Koren Dec., at ¶ 7. Relying on this misinformation, Vogt filed his 1981 personal tax returns, reflecting the erroneous figures. However, Vogt did not realize §751 ordinary income for the 1981 tax year due to WLKT's liquidation and, in fact, incurred instead a $15,127 long-term capital loss, as reflected in an "amended" Schedule K-1 which Vogt belatedly received from Abish on February 6, 1985, subsequent to initiation of this litigation. *See* Ex. 4; Vogt Aff., at ¶ 12; Koren Dec., at ¶ 6; Tr. 71-74.

After receiving the amended Schedule K-1 from Abish, Vogt initially assumed that defendants had kept their promise

and filed an amended partnership return with corrected Schedules K-1, possibly rendering "moot[ ]" a part of the litigation, but "[o]ut of an abundance of caution [he]...ask[ed] defendants in writing [the same day] whether the 'amended' Schedule K-1 had been filed." Vogt Aff., at ¶ 13; Ex. 5; Vogt Memo of Law, at 6. Nearly a month later on March 2, 1985, defendants responded, not to Vogt's precise question, but, rather, that they were "in the process of putting together the information you requested and will have same sent to you no later than March 20, 1985." Ex. 6; Tr. 74. However, Vogt did not just dutifully wait for "the information," but rather, astutely, made a direct inquiry to the taxing authorities on February 22, 1985 as to whether an amended partnership return with corrected Schedules K-1 had been filed. Exs. 7 and 9. The Internal Revenue Service ("IRS") responded in a letter, dated March 25, 1985, stating: "We have no record of ever receiving an ammended (*sic.*) return."[2] Ex. 8; Tr. 73-74. The defendants never responded to Vogt's inquiry by March 20, 1985, as promised, or on any other date; Vogt's time to file an amended personal tax return for the 1981 tax year and parallel refund claim expired on April 15, 1985. *See* Vogt Aff., at ¶¶ 15-16; Tr. 73-74.[3]

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[2] Vogt also wrote to the New York State Department of Taxation and Finance questioning whether an amended WLKT partnership return was filed. No reply, however, appears in the record, and Vogt states, none was received. *See* Ex. 9; Vogt Aff., at ¶ 15.

[3] 26 U.S.C. § 6511(a) permits a "[c]laim for credit or refund of an overpayment of any tax . . . [if] filed . . . within 3 years from the time the return was filed or 2 years from the time the tax was paid, whichever of such periods expires the later. . . ." "[A]ny return filed before the last day prescribed for the filing thereof shall be considered as filed on such last day." 26 U.S.C. § 6513(a). Accordingly, Vogt's 1981 tax return is deemed filed on April 15, 1982 and pursuant to § 6511(a), he had until April 15, 1985 to file a refund claim. However, Vogt could not request the refund until an amended 1981 WLKT partnership return with amended Schedule K-1's for each partner was filed and that amended return was never filed by defendants. As aforesaid, not until sometime after March 25, 1985, did Vogt learn from the IRS, by its letter of March 25, 1985, that no amended partnership return was filed. But even then, Vogt could not file an amended partnership return for the cogent reasons stated in his letter to the Magistrate, dated September 25, 1986, at 3-5.

In addition to the tax consequences resulting from the $20,000 posting error, Vogt justifiably claims that the error caused him to receive less than his fair share of partnership distributions. Specifically, he claims he is entitled to receive an additional $8,897, representing underpaid 1981 distributions (Koren Dec., at ¶¶ 13-14), and $3,168, as his share of the $25,000 May 14, 1982 distribution from which he alleges he was erroneously excluded. *Id.*, at ¶ 19; Ex. 15.

As to the final distribution on August 24, 1983, totalling $15,041, Vogt received $3,135, which, as we later note, represented an overpayment of $1,230; he should have received $1,905.

It is Vogt's deliberate exclusion from participation in the $25,000 May 14, 1982 distribution and Abish's failure to file an amended partnership return with corrected Schedules K-1, as promised, which principally underly his claim that punitive damages be assessed against the defendants. The $25,000 May 14 distribution was "made only to those partners who had a remaining cash basis capital amount" as of December 31, 1981. Ex. 15. But for the $20,000 posting error, Vogt correctly asserts that be would have had a positive capital balance as of December 31, 1981 and, therefore, would have been entitled to participate in the May distribution. *See* Koren Dec., at ¶¶ 15-19. Indeed, he maintains "Exhibit 13 establishes—as Mr. Koren confirms in ¶¶ 17-18 of his declaration—that defendants were fully aware of their posting error *six weeks earlier,* on April 2, 1982. . . .[and] [d]efendants' Exhibit 15 representation that plaintiff did not have a positive capital balance at 12/31/81 was thus a knowing and willful misrepresentation." Vogt Memo of Law, at 16-17. Exhibit 13 is dated April 2, 1982 and is entitled, "WLKT Computation of Distribution of Cash (1981). After Adj. of NJS/WHV." This " 'smoking gun' " memorandum, as Vogt terms it (*see* Vogt Memo of Law, at 7), was prepared by one "NS", presumably an MCC accountant. It represents, Koren declares, a "recalculation of capital balances" and "reflects defendants' recognition that Mr. Vogt did not in fact have a negative capital balance at the end of 1981, and

that he had instead been underpaid, rather than overpaid." Koren Dec., at ¶¶ 17-18; Tr. 131-134. Since this "recalculation" occurred prior to the May distribution, Koren states that Vogt should have received a 12.67% share, or $3,168. Koren Dec., at ¶¶ 16-19.

With respect to the amended Schedule K-1 Vogt received from Abish, Koren states:

> In my opinion, a client who receives a federal tax form such as the "amended" Schedule K-1 Mr. Vogt received, from certified public accountants who are additionally acting as liquidation fiduciaries, is fully entitled to understand that it is genuine and that it has been filed.

Id., at ¶11; *also* Tr. 201-202. He regards Abish's conduct of providing Vogt with an unfiled tax form as improper and the impropriety is exacerbated by his failure to respond to Vogt's written inquiry as to whether the amended Schedule K-1 had, in fact, been filed. Koren Dec., at ¶11.

Lastly, DiBenedetto, who is a professor of accounting at Pace University in Pleasantville, New York, a certified public accountant, and a certified management accountant and attorney, as well, testified as to the propriety of the defendants' conduct. Tr. 167. We shall discuss his testimony at greater length in our discussion of punitive damages.

VOGT'S DAMAGES

The defendants' liability is established by their default and only the "quantum" of damages need be determined. *Flaks v. Koegel,* 504 F.2d 702, 707 (2d Cir. 1974). All well-pleaded factual allegations of the Complaint are deemed admitted. *Au Bon Pain Corp. v. Artect, Inc.,* 653 F.2d 61, 65 (2d Cir. 1981); *Securities and Exch. Com'n v. Management Dynamics, Inc.,* 515 F.2d 801, 814 (2d Cir. 1975); *Trans World Airlines, Inc. v. Hughes,* 449 F.2d 51, 69 (2d Cir. 1971), *rev'd on other grounds,* 409 U.S. 363 (1973). In accepting, as we do, Vogt's well-pleaded allegations as true, causes of action for breach of

contract (Counts I and II), malpractice and negligence (Count III) and breach of fiduciary duties and fraud (Count IV) are deemed established for liability purposes. On his breach of contract claim Vogt is entitled to be put in as good a position as he would have been if the defendants abided by the contract. *Wallace Steel, Inc. v. Ingersoll-Rand Co.,* 739 F.2d 112, 115 (2d Cir. 1984); *Madison Fund, Inc. v. Charter Co.,* 427 F.Supp. 597, 608 (S.D.N.Y. 1977). The measure of damages on his tort and fraud claims is the "actual pecuniary loss sustained as a direct result of the wrong." *Accusystems Inc. v. Honeywell Information Systems,* 580 F.Supp. 474, 483 (S.D.N.Y. 1984); *also Lehman v. Dow Jones & Co., Inc.,* 783 F.2d 285, 296 (2d Cir. 1986); *Idrees v. American University of the Caribbean,* 546 F.Supp. 1342, 1350 (S.D.N.Y. 1982); 10 J. Fuchsberg, *Encyclopedia New York Law—Damages,* §842, at 352 (1965). Moreover, Vogt is entitled to prejudgment interest on his claims pursuant to New York Civil Practice Law and Rules ("CPLR") §5001(a) and "from the earliest ascertainable date the cause of action existed . . ." CPLR §5001(b); *Quintel Corp. v. Citibank, N.A., 606 F.Supp. 898, 913-914 (S.D.N.Y. 1985).*

COMPENSATORY DAMAGES—DEFICIENT DISTRIBUTIONS

As the result of MCC's accounting errors, Vogt did not receive the $6,000 distribution allocated to him in January 1981. *See* Ex. 11; Vogt Aff., at ¶ 7; Complaint, at ¶ 12(a). Koren confirms that his examinations of MCC's checks to Vogt did not include the $6,000 distribution and defendants could not produce a cancelled check therefor. Koren Dec., at ¶ 4; Tr. 122. Accordingly, Vogt is entitled to payment of $6,000, with prejudgment interest calculated from January 1, 1981 to the date judgment is entered. Pursuant to CPLR §5004, the annual rate of interest up to and including June 24, 1981 was 6%; effective June 25, 1981 and thereafter, the rate is 9%. *Quintel Corp. v. Citibank, N.A., supra,* 606 F.Supp., at 915.

Vogt further claims, and we agree, that because of an $20,000 posting error, he did not receive his rightful share of

1981 partnership distributions and was entirely excluded from the $25,000 May 14, 1982 distribution. As aforementioned, as for the last distribution of WLKT proceeds on August 24, 1983, Vogt received $3,135, representing a $1,230 overpayment, due to defendants recognition that "he had previously been underpaid." Koren Dec., at ¶¶ 12-14, 19, 20; Vogt Memo of Law, at 17. Accordingly, as to this last distribution, Vogt should have received only $1,905.

According to Koren, Vogt was entitled to receive a 12.67% share of all partnership distributions upon dissolution of WLKT. This figure is derived from Exhibit 12 and represents "[t]he sum of Mr. Vogt's opening capital balance at 1/1/81 (first column of figures) plus income allocated to him in 1981 (second column of figures), . . . [divided by] the partnership total of those items." Koren Dec., at ¶ 13. Koren asserts, "[u]pon liquidation of a partnership the proper and established accounting method for distributing available net cash to the partners is in proportion to there respective capital shares." *Id.*, at ¶ 12; Tr. 127-131, 171-174. Had defendants used this accounting method in distributing partnership proceeds, Koren maintains that Vogt should have received $299,736, that is, taking the 1981 total partnership distributions of $2,365,713 (column 3 of Ex. 12), multiplied by his aforesaid percentage share of 12.67%. Koren Dec., at ¶ 14. In fact, however, Vogt actually received only $290,839 ($310,839 less $20,000 posting error, *see* Ex. 12), thus, entitling him to the difference, namely, $8,897. *Id.* We accept Koren's calculations in light of our independent examination of the accounting records and the credence we give Vogt's qualified expert. Accordingly, we agree that Vogt is entitled to $8,897, with prejudgment interest computed on this amount from January 1, 1982.[4]

As for the $25,000 May 14, 1982 distribution, from which Vogt was entirely excluded, Koren calculates his 12.67% share

[4] Prejudgment interest should be calculated from January 1, 1982 because that is the earliest date Vogt's causes of action arose against defendants for their failure to pay him his fair share of *1981* partnership distributions.

as $3,168. *See* Koren Dec., at ¶19. Only WLKT partners with a positive capital balance as of December 31, 1981 were to participate in the May distribution. *See* Ex. 15. But for defendants' posting error, we agree Vogt would have had a positive capital balance as of December 31, 1981 and was thus entitled to his share of this distribution of partnership proceeds. Koren Dec., at ¶¶ 17-18; Tr. 49. Accordingly, Vogt is due this amount; however, because defendants paid Vogt a 20.84% share of the $15,041 August 24, 1983 distribution, instead of a 12.67% share, to which he was entitled, the amount overpaid, namely $1,230, should be setoff against the $3,168 Vogt should have received in May 1982. Thus, Vogt is entitled to collect from defendants for deficient 1982 partnership distributions, a total of $1,938, ($3,168 less $1,230), with prejudgment interest calculated from May 14, 1982. Koren Dec., at ¶20.

EXCESSIVE INCOME TAXES

In addition to the $20,000 posting error, resulting in Vogt not receiving his fair share of partnership distributions, he was caused to overstate his taxable income for the 1981 tax year and, thus, he paid excessive taxes. As discussed, the amended Schedule K-1, which Vogt received from Abish on February 6, 1985, reveals that as the result of WLKT's liquidation he did not realize $4,873 as § 751 ordinary income, as initially reported (*see* Ex. 3), but, in fact, it states that Vogt incurred a $15,127 long-term capital loss. *See* Ex. 4; Tr. 77. In his declaration, Koren has calculated the amount of excessive taxes paid by Vogt because of the posting error for the 1981, 1982 and 1983 tax years.

A. *1981 Tax Year*

Had the figures appearing in the amended Schedule K-1 been reported timely and properly to Vogt in the first instance, Koren states Vogt's taxes would have been significantly reduced, for the following reasons:

(a) his taxable income would have been reduced by eliminating the item of § 751 ordinary income;

(b) his taxable income would have been reduced by reason of the capital loss newly reported in Exhibit 4;

(c) his 1981 federal income tax would have been reduced by reason of (a) and (b); and

(d) the decrease in tax would have reduced the amount of the Form 2210 charge he paid.

See Koren Dec., at ¶ 7. The foregoing translates into a $4,648.39 reduction in 1981 federal income taxes. *Id.* Accordingly, Vogt is entitled to this amount, together with prejudgment interest computed from April 15, 1982 to the date judgment is entered, at IRS refund rates, which are higher than the CPLR's 9% prejudgment interest rate, which would otherwise apply.

CPLR § 5004 provides that "[i]nterest shall be at the rate of nine per centum per annum, except *where otherwise provided by statute.*" (emphasis added). The legislative purpose of the CPLR's interest provisions "is to put the aggrieved party in as good a position as performance would have done." *Bulk Oil (U.S.A.), Inc. v. Sun Oil Trading Co.*, 697 F.2d 481, 485 (2d Cir. 1983). "[T]he rate used in computing statutory interest is an *assumption* about the value of the use of money." *Id.* (emphasis in original). When a more accurate rate exists reflecting the true loss, that rate should be used in lieu of the statutory rate. *Cf. id.; Rios v. Enterprise Ass'n. Steamfitters Local 638,* 651 F.Supp. 109, 115 (S.D.N.Y. 1986) (adjusted prime rate provided in 26 U.S.C. § 6621 used to fix rate of prejudgment interest, as opposed to CPLR § 5004, "to make whole the victims of racial discrimination."). Here, had defendants performed as they promised and filed an amended partnership return, Vogt could have obtained a tax refund together with interest at the respective IRS rates "from the date of the overpayment [of taxes] to a date. . .preceding the date of the refund check by not more than 30 days. . . ." 26 U.S.C. § 6611(b)(2). While the date of overpayment is ascertainable,

April 15, 1982,[5] any attempt on our part to predict when the IRS would have processed Vogt's refund, had he filed an amended return, would be speculative. However, we believe it is better to speculate in this regard than to run the risk of undercompensating Vogt for his loss, against which defendants have turned a blind eye and deaf ear. As our Circuit has repeatedly stated:

> "The rule which precludes the recovery of uncertain damages applies to such as are not the certain result of the wrong, not to those damages which are definitely attributable to the wrong and only uncertain in respect of their amount." *Story Parchment Co. v. Paterson Co.*, 282 U.S. 555, 562 . . . (1931).

Compania Pelineon De Navegacion v. Texas Pet. Co., 540 F.2d 53, 55-56 (2d Cir. 1976), (Brieant, J.), *cert. denied*, 429 U.S. 1041 (1977); *also generally Burndy Corp. v. Teledyne Industries, Inc.*, 748 F.2d 767, 771 (2d Cir. 1984) ("[A] court may engage in some degree of speculation in computing the *amount* of . . . damages . . . [once] causation [is] established.") (emphasis in original); *S. Leo Harmonay, Inc. v. Binks Mfg. Co.*, 597 F.Supp. 1014, 1030 (S.D.N.Y. 1984), *aff'd*, 762 F.2d 990 (2d Cir. 1985) ("[C]ourts have recognized that a plaintiff may recover even where it is apparent that the quantum of damage is unavoidably uncertain, beset by complexity, or difficult to ascertain, if the damage is caused by the wrong. As the New York Court of Appeals commented: 'The law is realistic enough to bend to necessity in such cases.' ") (cite omitted). Accordingly, prejudgment interest on Vogt's claim should be computed at the higher IRS rates and New York refund rates where applicable, from April 15, 1982 to the date judgment is entered, compounded daily where indicated, *see* 26

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[5] As aforesaid, prepaid estimated tax and tax withheld at the source are deemed paid on the last day prescribed for filing a return. *See* n.3, *supra*. Thus, taxes paid by Vogt for the 1981 tax year are deemed paid on April 15, 1982. Prejudgment interest should be computed from this date. *See* 14 Mertens, *Law of Federal Income Taxation*, § 58.48, at 171 (1984 ed.) ("Mertens").

U.S.C. §6622(a) (West Supp. 1986); we set forth the applicable IRS rates in the footnote.[6] Vogt (Pl's Memo, at 10) and his accountant (Koren Dec., at ¶22) also soundly argue for the higher interest rates.

Koren examined Vogt's 1981 New York State income tax return and has calculated the tax savings as $349.68, had the "amended" and corrected Schedule K-1 figures been used. We accept the same. Accordingly, Vogt is also entitled to this amount, together with interest from April 15, 1982, through the date judgment is entered at New York State tax refund rates for the reasons stated above. *See* Koren Dec., at ¶8. We set forth the applicable New York State refund rates in the footnote.[7]

B. *1982 and 1983 Tax Years*

Koren asserts that "[b]ecause IRS regulations would not have permitted Mr. Vogt to deduct the full amount of the capital loss on his 1981 return, a portion of the loss (which I calculate to be $10,877) would have been carried forward to

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[6] The rate of interest on overpayments of federal tax for the relevant periods herein, is as follows:

February 1, 1982	to December 31, 1982	20%
January 1, 1983	to July 1, 1983	16%
July 1, 1983	to December 31, 1985	11%
January 1, 1986	to June 30, 1986	10%
July 1, 1986	to December 31, 1986	9%
January 1, 1987	to June 30, 1987	10%

See Mertens, *supra*, §58A.44 (and February 1987 supplement); J.K. Lasser's, *Your Income Tax*, Prentice Hall Press (1987), at 248. Interest is compounded daily only from January 1, 1983. *See* 26 U.S.C. §6622(a) (West Supp. 1986, Notes).

[7] The rate of interest for the overpayment of New York State income tax for the relevant periods herein, is as follows:

April 15, 1982	to February 28, 1983	13.5%
March 1, 1983	to February 29, 1984	9.1%
March 1, 1984	to February 28, 1986	10.0%
March 1, 1986	to February 28, 1987	7.9%
March 1, 1987	to February 28, 1988	6.0%

See 2 State and Local taxes, New York, §603.2, at 65.322 (Prentice Hall 1981). Interest is compounded daily only from September 1, 1983. *Id.*, §603.2.20, at 65.322-A.

his 1982 federal return and been available to offset a like amount of short-term capital gains, thereby providing tax-sheltered income." Koren Dec., at ¶9; *see* 26 U.S.C. §§1211(b), 1212(b). No short-term capital gains, however, were generated by Vogt for the 1982 tax year. Vogt states:

> Had the Schedule K-1 tax return materials furnished to me by defendants in early 1982 reflected [the $15,127] capital loss, as they should have, I would have taken steps to incur off-setting short-term capital gains, as I was in a position to do, thereby obtaining tax-sheltered income.

Vogt Aff., at ¶17. In order to fully utilize the carry-over loss, Vogt had to be in a position to generate $10,877 in short-term capital gains. *See* Vogt's Affidavit, sworn January 13, 1987, ¶7 ("Vogt Aff. No. 2"); Tr. 153. In fact, Vogt has established that as of May 1982, he could have generated roughly $8,200 in short-term capital gains. Vogt Aff. No. 2, ¶¶3-7; Exs. 49-52. The remaining $2,677 in short-term gains, he claims, he could have "readily . . . incurred" in light of the "sharply rising" stock and bond market during the remaining months of 1982. Vogt Aff. No. 2, ¶7; Tr. 83-88. It is clear that Vogt is a sophisticated investor and thus we credit his assertion that he could and would have generated the additional, relatively small sum of $2,677 in short-term capital gains to fully utilize the carryover loss on his 1982 federal tax return. Federal tax savings from the 1982 tax year, had Vogt been able to utilize the carryover loss, would have totalled $5,438.50. Koren Dec., at ¶9. Connecticut* tax savings would have totalled $761.39. *Id.* Accordingly, he is due these amounts, with interest from April 15, 1983, the date Vogt's 1982 taxes are deemed paid by the taxing authorities. *See* 26 U.S.C. §6513.[8]

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* Vogt resides in Connecticut.

[8] Since our award of tax benefits, Vogt would have enjoyed in his 1982 tax year, had he utilized the federal carryover loss for that year, does not represent a refund of an overpayment of tax, interest on these amounts should be calculated at 9%.

Additionally, for the 1982 tax year, Koren states that Vogt would have had a New York capital loss carryover of $9,127, which he *could have utilized*, irrespective of the generation of short-term capital gains,[9] "to offset $3,000 of 1982 New York [ordinary] income . . . and $1,564 of 1983 New York [ordinary] income." Koren Dec., ¶10. Consequently, he would have paid $407.96 less New York income tax in 1982 and $137.90 less tax in 1983. *Id.* These amounts too are properly due Vogt with interest at New York refund rates, to the extent they exceed the 9% CPLR rate. Interest should be computed from the dates the overpayments occurred, April 15, 1983 and April 15, 1984, respectively, to the date judgment is entered.

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[9] Irrespective of the generation of short-term capital gains in the 1982 tax year, Vogt could have set off half of his long-term carryover loss up to $3,000 of ordinary income on his New York State return. *See* 26 U.S.C. §1211(b). The New York Tax Law ("TL") operates in conformity with federal law, but limits a nonresident's recognition of capital gains and losses to those derived from New York State sources. *See* TL §§632(a)(1), (b)(1); 20 N.Y.C.R.R. §131.7. An example is helpful:

> Taxpayer A, a nonresident of New York State for the entire taxable year 1982, had a long-term capital gain from sources without New York State (from the sale of securities) of $20,000 on his Federal income tax return. A also included on his Federal income tax return a long-term capital loss of $8,000 from sources exclusively within New York State (from the sale of owned rental property). For Federal income tax purposes, A has a gain from the sale or exchange of property of $12,000 ($20,000 minus $8,000). On his New York State nonresident personal income tax return, A has only a long-term capital loss of $8,000 as this is the only capital item derived from New York State sources. A is allowed to claim a maximum capital loss deduction of $3,000 on his 1982 New York State nonresident personal income tax return and is allowed a $2,000 long-term capital loss carryover for the following year for New York State personal income tax purposes even though his 1983 Federal income tax return will show no capital loss carryover.

Id., at §131.7(c)(1); *also* Letter to Magistrate from Vogt, dated December 2, 1986.

LEGAL AND ACCOUNTING FEES

Vogt seeks "legal and accounting fees and expenses which [he has] incurred, but would not have incurred but for defendants' acts and omissions complained of." Vogt Aff., at ¶23. Vogt does not set forth the legal authority for such claims.

A. ***Accounting Fees:***

Since we are aware of no federal or state statutory authority, permitting an award of a party's accounting fees, under the circumstances presented here, and Vogt cites none, we presume that Vogt seeks these fees as part of his claim for compensatory damages—i.e., as damages proximately caused by defendants' negligence and breach of contract. We found but one older New York case of a lower court which recognized, as justified, an award of accounting fees on this basis. *See Block, Inc. v. Klein,* 45 Misc. 2d 1054, 1059-1060, 258 N.Y.S. 2d 501, 508 (Sup. Ct., N.Y.Co., 1965) (Court awarded "(1) the accounting and auditing fees paid to defendants for the one year of services rendered by them immediately prior to the issuance of the erroneous balance sheet . . . and (2) the accounting and auditing fees necessitated by the review of this erroneous statement . . . [as damages] flow[ing] naturally, directly, and solely from defendants' negligence or their breach of contract. . . . "). These accounting fees, incurred as the proximate result of defendants' negligence or breach of contract, necessarily must be separated from those fees incurred by Vogt in preparation for the this litigation. *See Union Carbide and Carbon Corporation v. Nisley,* 300 F.2d 561, 586-587 (10th Cir. 1961), *cert. denied,* 371 U.S. 801 (1962) (accounting fees incurred in connection with prosecution of case not allowable as costs); *Helfer v. Corona Products,* 127 F.2d 612, 623 (8th Cir. 1942) (same).

From our review of the statements for accounting services exhibited by Vogt, it appears that only the statement dated February 25, 1983, totalling $1,686, was connected with Koren's review of MCC's distribution or partnership proceeds.

The other statements exhibited post-date the filing of the lawsuit on January 3, 1985, and the accounting services therein, without further elucidation, must be presumed to have been rendered in connection with the lawsuit. *See* Exs. 20, 56. Thus, we would normally allow Vogt $1,686 for accounting services incurred as the proximate result of the defendants' negligence and breach of contract, as distinguished from accounting services performed in preparation for this litigation, which we would not allow. However, we do not allow the $1,686 costs, because nowhere does Vogt set forth Koren's rate of compensation or detail the accounting services rendered. (The February 25, 1983 statement, for example, merely sets forth the sum $1,686 for "Representation in connection with distribution of partnership interest from Watson et al.". *See* Ex. 20). Without this detailed information, we cannot indulge in any meaningful examination of the reasonableness of the services provided and charges made. Accordingly, Vogt should not be reimbursed for any of the accounting costs. Of course, to the extent Vogt may be entitled to witness fees relative to the testimony at the hearing of experts, Messrs. Koren and DiBenedetto, pursuant to 28 U.S.C. §1821, they should be deemed taxable costs. *See Warner Bros. Inc. v. Gay Toys, Inc.*, 598 F.Supp. 424, 432 (S.D.N.Y. 1984).

Legal Fees:

Vogt submits a bill for $705 from a law firm, for consulting with Vogt and reviewing the complaint.

While we sympathize with Vogt for the amount of time MCC's reckless omissions necessarily detracted him from his work as a distinguished patent attorney, nevertheless, in our Circuit, absent express statutory authority, the " 'American Rule' " precludes the "prevailing party in federal court litigation [from] recover[ing] [his] attorneys' fees . . . ." *Dow Chemical Pacific Ltd. v. Rascator Maritime S.A.*, 782 F.2d 329, 344 (2d Cir. 1986) (citing *Alyeska Pipeline Service Co. v. Wilderness Society*, 421 U.S. 240, 247 (1975)). While there are several exceptions to the American Rule, *see Alyeska Pipeline*

Service Co., supra, at 257-259; *e.g., Dow Chemical, supra,* at 344-345, Vogt does not alert us to the basis, if any, underlying his claim for attorney's fees; nor is the existence of an applicable exception apparent from the record or other papers relevant to this action. We would disallow this item.

PUNITIVE DAMAGES

Lastly, we address Vogt's claim that punitive damages be assessed against the defendants. Pursuant to New York law, which necessarily guides us in this diversity action, punitive damages are not awarded as a matter of right, but lie within the sound discretion of the trier of fact. *Whitney v. Citibank, N.A.,* 782 F.2d 1106, 1118-1119 (2d Cir. 1986); *Flaks v. Koegel, supra* 504 F.2d, at 707; *Meehan v. Snow,* 494 F.Supp. 690, 696 (S.D.N.Y. 1980). They are generally allowed "where the defendant's conduct amounts to such gross, wanton or willful fraud, dishonesty, or malicious wrongdoing as to involve a high degree of moral culpability, making it appropriate to deter the defendants from engaging in similar conduct in the future and to induce the victim to take action against the wrongdoer." *Whitney v. Citibank, N.A., supra* at 1118 (*citing Walker v. Sheldon,* 10 N.Y.2d 401, 404-405 (1961)). In the words of the New York Court of Appeals, " '[i]t is not the form of the action that gives the right to the [trier of fact] to give punitory damages, but the moral culpability of the defendant.' " *Walker v. Sheldon, supra,* at 404-405 (*quoting Hamilton v. Third Avenue Railroad Co.,* 53 N.Y. 25, 30 (1873)); *Whitney, supra,* at 1118 ("The test is not the number of wrongful acts but whether the conduct is sufficiently willful and egregious to indicate a need for something more than compensatory relief."). Significantly, *Whitney* also instructs us that "[punitive] damages have been [and can be] awarded for a single act of wrongoing (cases cited)," *id.,* a principle particularly applicable here. Conduct supporting an award of punitive damages is characterized alternatively as " 'utter recklessness,' " " 'reckless and of a criminal nature,' " " 'wanton or malicious,' " " 'gross and outrageous,' " " 'recklessly and wantonly,' " or

" 'close to criminality.' " *Brink's Inc. v. City of New York,* 546 F.Supp. 403, 411 (S.D.N.Y. 1982), *aff'd,* 717 F.2d 700 (2d Cir. 1983) (*quoting Roginsky v. Richardson-Merrell, Inc.,* 378 F.2d 832, 842-843 (2d Cir. 1967)).

In assessing punitive damages against a business entity, it is singularly significant to note that such an award is "intended to inject an additional factor into the cost-benefit calculations of companies who (*sic.*) might find it fiscally prudent to disregard the threat of liability." *Doralee Estates v. Cities Service Oil Co.,* 569 F.2d 716, 723 (2d Cir. 1977); *cf. Walker v. Sheldon, supra,* at 406. However, before awarding punitive damages against a corporate or other business entity, a court must satisfy itself that " 'the continuing tortious conduct has been brought home to the consciousness of relatively important managerial personnel with authority to make a decision for the corporation that would have prevented the damage.' " *Brink's Inc. v. City of New York,* 717 F.2d 700, 705 (2d Cir. 1983) (*quoting Doralee, supra,* at 722). "New York, in other words, adheres to the 'complicity rule,' holding the corporate master liable for punitive damages 'only when superior officers either order, participate in, or ratify outrageous conduct.' " *Roginsky, supra,* 378 F.2d, at 842 (cite omitted); *Aldrich v. Thomson McKinnon Securities, Inc.,* 756 F.2d 243, 247 (2d Cir. 1985).

Allegations of malicious conduct appearing in the complaint are not accepted as conclusive by virtue of the default judgment; they must be proven to the satisfaction of the court before punitive damages are justified. *Flaks v. Koegel, supra,* 504 F.2d, at 707; *Deshmukh v. Cook,* 630 F. Supp. 956, 959-960 (S.D.N.Y. 1986); *Meehan v. Snow, supra,* 494 F.Supp., at 697-698.

Vogt asserts that the defendants' knowing exclusion of him from participation in the $25,000 May 1982 distribution (*see* Vogt's Memo of Law, at 16-17) and their failure to file an amended partnership return with corrected Schedules K-1 (*see id.,* at 17-19) constitute willful, wanton and malicious acts and "outrageous conduct," justifying an award of punitive damages. We address these alleged acts of misconduct in *seriatim.*

The May 1982 Distribution:

As Vogt contends, and we agree, Exhibit 13 establishes that someone in MCC was apparently aware of the $20,000 posting error and made an adjusting entry on April 2, 1982, nearly six weeks prior to the May 14, 1982 distribution. We do not agree, however, that such knowledge warrants the imposition of punitive damages against the defendants. Firstly, Exhibit 13 was prepared by one "NS," ostensibly not Sheldon Abish; nor may we assume that "NS" is another principal of MCC. Vogt does not allege that Abish himself was apprised of or had actual knowledge of the posting error before the distribution; nor does it appear in the record that knowledge of the error was " 'brought home to the consciousness of relatively important managerial personnel with authority to make a decision for the corporation. . . .' " *Brink's, supra,* 717 F.2d, at 705 (cite omitted). It is inferrable, and likely, probable, that "NS" who prepared Exhibit 13 (whose name or position at MCC is not known to Vogt, Tr. 95) informed Abish or other important managerial personnel of the error (TR. 231-232); however, assuming exclusion from the May 1982 distribution in the face of such knowledge would constitute "recklessness. . . close to criminality," nevertheless, such recklessness must be " 'clearly established.' " *Roginsky, supra,* 378 F.2d, at 843. Here, Vogt has failed to *clearly establish* Absih's personal knowledge of the error prior to the May 1982 distribution or the personal knowledge of a similarly responsible MCC official. While it may be reasonable to charge the principals of MCC with knowledge of the error no later than April 2, 1982 for the purpose of establishing their malpractice, we hesitate to engage in the same presumption as support for an award of punitive damages. (*See* Tr. 231-232). Yet, there are other reasons for denying punitive damages to Vogt for his exclusion from the May 1982 distribution.

Equally significant, in Vogt's own words, is defendants' attempt "to make up for their [erroneous exclusion of Vogt from participation in the May 1982 distribution by] recalculat[ing] plaintiff's capital share at 12/31/81 as 20.84%, rather

than as a negative figure (Koren ¶ 17; Exhibit 14)." Vogt Memo of Law, at 17. Koren states, defendants "distributed a 20.84% share [of the $15,041 August 24, 1983 distribution] to [Vogt], amounting to $3,135, recognizing that he had previously been underpaid"; Vogt should have only received $1,905 as his 12.67% share of that distribution. Koren Dec., at ¶ 20. The defendants' attempt to make up for their error belies "malicious wrongdoing," "a high degree of moral culpability" or "evil motives," necessary prerequisites for an award of punitive damages. *Whitney v. Citibank, N.A., supra,* 782 F.2d, at 1118; *Accusystems, Inc., supra,* 580 F.Supp., at 483. Rather, in this regard, defendants' conduct appears at most negligent. Punitive damages are inappropriate "where there is only negligence or poor judgment on the part of the defendant." *Meehan v. Snow, supra,* 494 F.Supp., at 697.

Defendants' Failure to File an Amended Partnership Return:

As a "further instance of malicious conduct," Vogt states that defendants became aware of the $20,000 posting error as early as April 2, 1982 and did not communicate this information to him, but "maintained their silence, and thereby deliberately cause[d] plaintiff to pay more in taxes than he should have, their professional and fiduciary obligations to plaintiff notwithstanding." Vogt Memo of Law, at 17-18. Had defendants acted as they should have, Vogt asserts, he could have obtained an extension of time from the taxing authorities to file his personal returns and avoided payment of excessive taxes. *Id.* Moreover, Vogt highlights defendants' unfulfilled promise in January 1983 to file an amended partnership return with corrected Schedules K-1 and Abish's transmission of an amended, but unfiled, Schedule K-1 to Vogt soon after commencement of the litigation. *Id.,* at 18-19. He claims the sending of the amended Schedule K-1 by Abish, "which on its face it appeared to be genuine, along with defendant Abish's transmittal note reading, 'Enclosed is your revised K-1' " was a "snare and delusion, a sham. . . ." *Id.,* at 19. The defendants' malicious conduct, Vogt asserts, demonstrates fraud, constructive fraud, breach of fiduciary duty and evinces "a disingenuous

or dishonest failure to carry out a contract," justifying an award of punitive damages. *Id.*, at 12-24. We agree that defandants' conduct in this regard merits significant punitive damages.

Vogt has established that defendants were apprised of the $20,000 posting error and its concomitant tax consequences by Koren as early as 1982. *See* Koren Dec., at ¶5. Indeed, the error was again acknowledged to Vogt at the January 24, 1983 meeting with Abish and Koren. *Id.;* Vogt Aff., at ¶9; Ex. 17. In a contemporaneous memo of a telephone conversation, dated January 19, 1983, Vogt recorded Abish's personal concession that the $20,000 item was erroneously posted to his drawing account and Abish's promise to file an amended partnership return with corrected Schedules K-1 for himself and Stathis. *See* Ex. 17. However, an amended partnership return was never filed by MCC, precluding Vogt from obtaining federal and state tax refunds, despite the fact that MCC had over two years, until April 15, 1985, to do so. While Abish sent Vogt an amended Schedule K-1 several months after initiation of this action, for some bewildering reason defendants never filed it. *See* Exs. 4, 7-9. When Vogt attempted to ascertain from Abish whether and when, in fact the amended K-1 was filed, he received no reply to his specific inquiry, but, rather, received a meaningless note from Abish, dated March 2, 1985, that he, Abish, is "putting together the information you requested and will have same sent to you no later than March 20, 1985." *See* Vogt Aff., at ¶¶12-16; Exs. 5, 6.

Ordinarily, an accountant who prepares erroneous financial statements, injurious to his client, is guilty of, at most, negligence or malpractice. Where, however, the accountant is apprised of an accounting error, and promises his client to take steps to correct or mitigate the error, as here, but deliberately fails to take such steps, resulting in serious financial prejudice to that client, we submit that such behavior is not mere negligence but, rather, should be characterized as no less than grossly negligent and reckless, deserving of severe condemnation. (*See* Tr. 197-199). The dereliction is compounded even further

when the accountant stands in a fiduciary relationship with the client, as here. Indeed, under New York law, an "unfulfilled promise . . . made by a defendant who shares a confidential or fiduciary relationship with the plaintiff" alone constitutes constructive fraud. *Brown v. Lockwood,* 76 A.D.2d 721, 733-734 (2d Dept. 1980).

It must be clearly understood that not only were the defendants acting as certified public accountants, subject to the strict ethical precepts appearing in their "code of ethics" (*see* Ex. 24), but as liquidation fiduciaries as well. (Tr. 175, 205). Professor DiBenedetto outlined several of the defendants' many code violations. For instance, the defendants' doning of several hats—by acting as WLKT's public accountant, bookkeeper, and liquidation fiduciary—violates this "basic tenet" of the accounting profession: "A certified public accountant should maintain his integrity and objectivity and, when engaged in the practice of public accounting, be independent of those he serves." Ex. 24, ET 51.07; Tr. 179-184. This "basic tenet" is also violated by the defendants' representation of some, but not all, of WLKT's partners, while also acting as liquidation fiduciaries; such fiduciaries, in Professor DiBenedetto's words, "must behave as Caeser's wife. [They] must be beyond reproach." (Tr. 186-187).

More central to the propriety of a punitive damage award, and most troubling to the Professor, was the defendants' sending to Vogt an unfiled Schedule K-1 with a note, "Enclosed is your revised K-1." We agree that a client can draw no other inference from receipt of such a tax form but that it was filed. The Professor characterizes defendants' conduct as deliberate deception, a "lie," violative of ET 54.04's cardinal principle that "[a] CPA should be frank and straightforward with clients." *See* Ex. 24, at 4321; Tr. 201-203. This deriliction was compounded by the defendants' failure to respond to Vogt's inquiry, which exhibits, at best, eminently reckless behavior. Tr. 212-213. Lastly, the Professor opined, that the $20,000 misposting was negligence, but the failure to remedy the error upon its discovery, and disclose this information to the other

partners of the firm, can be best characterized as grossly negligent. Tr. 197. We would characterize such conduct also in different terms; it constituted the most hightened indifference to their professional responsibilities.

We find the conduct of a certified public accounting firm, the substantial size of MCC (*see* Ex. 43), unexplainable except in terms of extraordinary recklessness and of gross indifference to and disregard of Vogt's interests and rights. The *only* inference to be drawn from the facts is that the defendants, fully aware that their failure to file an amended partnership return would preclude Vogt from obtaining a tax refund, consciously, intentionally and wilfully chose to interfere with his rights by failing to act, their fiduciary responsibilities notwithstanding. The facts here strike us as precisely a case where the defendants cooly engaged in "cost-benefit calculations" and found it "fiscally prudent to disregard the threat of liability." *Doralee supra,* 569 F.2d, at 723; *Walker v. Sheldon, supra,* 10 N.Y.2d, at 406.

One of the principal salutary purposes for the imposition of punitive damages is to provide plaintiffs with an incentive to seek redress, even where wrongs may result in only minimal compensatory relief. *Whitney, supra,* 782 F.2d, at 1118. The defendants made a conscious decision, after they conceded their errors and promised to file an amended partnership return, not to follow through. It is possible, and from our perception of the facts, highly probable, that the defendants did not wish to alert other partners of the WLKT firm to their errors, because they desired to retain their continued business; Vogt was not one of their continuing clients after the law firm's dissolution. Furthermore, during 1983 the IRS examined WLKT's final 1981 partnership return and found it satisfactory. Tr. 63-66. It is within the realm of probability that the defendants believed that the filing of an amended return would trigger yet another audit; moreover, correction of the $20,000 error would affect all of the partners' K-1's and possibly require their personal returns to be amended, subjecting them to a possible future audit. Tr. 138-141. Thus, in the spirit of letting a sleeping bear

lie, the defendants conceivably decided it was more convenient and financially logical for them to give Vogt the proverbial runaround—and they did just that. Not only did they fail to file an amended partnership return as promised, but also they perpetuated their wrongs by failing to respond to Vogt's inquiries and, after initiation of the lawsuit, deliberately misled him by sending him an "amended" but unfiled K-1, which was all but worthless. On top of it all, the defendants did not answer the complaint, possibly realizing the absence of a valid defense and gambling on the improbability of an award of punitive damages, and never once attempted to settle the matter, or even discuss it with Vogt, as would be expected of any responsible professional who wronged a client. Their conduct cannot and must not be countenanced or pass without serious sanction imposed.

In *Aldrich v. Thomson McKinnon Securities, Inc., supra,* 756 F.2d, at 248, our Circuit was similarly irritated with a defendant brokerage's "grossly negligent" supervision of one of its employees, resulting in reprehensible churning of a client's investment funds. The Court recommended on remittitur a punitive damage award of 1.5 million dollars, recognizing that the defendants' "reckless[ ] disregard[ ]" of the manipulation of plaintiff's account should stand as a lesson to future violators. *Id.,* at 248-249. Although the Court was not directly faced with the issue, it noted that under New York law a "showing of a fraud on the public is no longer a prerequisite to the award of punitive damages." *Id.,* at 248, n.5 (*citing Borkowski v. Borkowski,* 39 N.Y.2d 982 (1976)); *Whitney, supra,* 782 F.2d, at 1118 (*citing* same). It held the brokerage's "wanton and reckless disregard of the trust placed in it by [plaintiff] was not only a wrong against her but, by what it portended for other unfortunate investors, it was a wrong against the general public." *Aldrich, supra,* at 249. We note, here too, that the defendants, as certified *public* accountants, would serve all the public who would pay its fees, and owes no lesser obligation to its individual clients than would a securities house, the likes of Thomson McKinnon.

Conduct such as that of the defendants' similiarly must be deterred and an award of punitive damages must be of sufficient substance to "make the offender 'smart.' " *Whitney, supra,* 782 F.2d, at 1119 (*quoting Reynolds v. Pegler,* 123 F.Supp. 36, 41 (S.D.N.Y. 1954), *aff'd,* 223 F.2d 429 (2d Cir.), *cert. denied,* 350 U.S. 846 (1955). "In determining the amount and effectiveness of exemplary damages to be awarded against a defendant, the court may take into consideration the defendant's wealth or net worth." *Id.* Recognizing MCC as a leading New York City certified public accounting firm, with nine partners and employing a total professional staff of 89 accountants, as of year-end 1986 (*see* Ex. 43), we submit that punitive damages in the sum of $150,000 is reasonable and appropriate.

SUMMARY OF DAMAGES

Vogt has been damaged as the result of MCC and Abish's conduct, as follows:

	Principal Amount	Interest Period			Rate
Federal Tax Consequences					
1981	$4,648.39	4/15/82	to	12/31/82	20.0%
		1/1/83	to	7/1/83	16.0% (CD)*
		7/1/83	to	12/31/85	11.0% (CD)
		1/1/86	to	6/30/86	10.0% (CD)
		7/1/86	to	12/31/86	9.0% (CD)
		1/1/87	to	6/30/87	10.0% (CD)
See n. 6					
1982	$5,438.50	4/15/83	to	Entry of Judgment	9.0%
See n. 8					
Connecticut Tax Consequences					
1982	$ 761.39	4/15/83	to	Entry of Judgment	9.0%

* "CD" denotes interest to be compounded daily.

	Principal Amount	Interest Period			Rate
New York State Tax Consequences					
1981	$ 349.68	4/15/82	to	2/28/83	13.5%
		3/1/83	to	8/31/83	9.1%
		9/1/83	to	2/29/84	9.1% (CD)
		3/1/84	to	2/28/86	10.0% (CD)
		3/1/86	to	2/28/87	7.9% (CD)
		3/1/87	to	2/28/88	6.0% (CD)
See n. 7					
1982	$ 407.96	4/15/83	to	8/31/83	9.1%
		9/1/83	to	2/29/84	9.1% (CD)
		3/1/84	to	2/28/86	10.0% (CD)
		3/1/86	to	2/28/87	7.9% (CD)
		3/1/87	to	2/28/88	6.0% (CD)
See n. 7					
1983	$ 137.90	4/15/84	to	2/28/86	10.0% (CD)
		3/1/86	to	2/28/87	7.9% (CD)
		3/1/87	to	2/28/88	6.0% (CD)
January 1981 Distribution	$6,000.00	1/1/81	to	6/24/81	6.0%
		6/25/81	to	Entry of Judgment	9.0%
Deficient 1981 Distribution	$8,897.00	1/1/82	to	Entry of Judgment	9.0%
Deficient 1982 Distribution	$1,938.00	5/14/82	to	Entry of Judgment	9.0%

* "CD" denotes interest to be compounded daily.

Further, punitive damages in the sum of $150,000.00, should be assessed against the defendants. All awards are to be assessed against defendants, jointly and severally.

RECOMMENDATION

In light of the above, a money judgment should be entered against the defendants MCC and Abish, jointly and severally, for the principal amounts set forth hereinabove, with pre-judgment interest computed at the rates above indicated, together with punitive damages in the sum of $150,000.00, and the costs and disbursements of this action.

Plaintiff shall submit to the Court a proposed judgment consistent with this Report and to the extent it is adopted by the Court.

NOTICE

Pursuant to 28 U.S.C. §636(b)(1)(C), as amended, and Rules 72(b), Fed.R.Civ.P. and 7 of this District's Rules for Proceedings Before Magistrates, the parties shall have ten (10) days, plus an additional three (3) days, pursuant to Rule 6(e), Fed.R.Civ.P., or a total of thirteen (13) working days, (*see* Rule 6(a), Fed.R.Civ.P.), from the date hereof, to file written objections to this Report and Recommendation. Such objections, if any, shall be filed with the Clerk of the Court, with extra copies delivered to the chambers of The Honorable Chief Judge Charles L. Brieant, Room 30, at the United States Courthouse, 101 East Post Road, White Plains, New York 10601, and to the chambers of the undersigned at the said courthouse.

A party who may feel aggrieved by a recommended decision herein and who fails to file timely objections thereto, waives any right to appellate review of the District Court's order (or judgment) entered relative hereto. *See Thomas v. Arn*, ___ U.S. ___, 106 S.Ct. 466 (1985); *McCarthy v. Manson*, 714 F.2d 234, 237 (2d Cir. 1983). Requests for extensions to file objections shall be made to the Judge and shall *not* be made with the Magistrate.

Dated: White Plains, New York
March 26, 1987

RESPECTFULLY SUBMITTED,

JOEL J. TYLER

Joel J. Tyler
United States Magistrate

Copy of the foregoing
REPORT AND RECOMMENDATION
has been mailed this day to:

William H. Vogt, III, Esq.
707 Westchester Avenue
White Plains, New York 10604

[Filed May 13, 1987]

United States District Court
Southern District of New York

WILLIAM H. VOGT III,

Plaintiff,

–against–

SHELDON ABISH and
MAHONEY, COHEN & CO., P.C.,

Defendants.

85 Civ. 0088 (CLB)

Memorandum and Order

Brieant, Chief J.

The Court has reviewed the Report and Recommendation of the Hon. Joel J. Tyler, United States Magistrate, filed herein on March 27, 1987 ("Report"), and the Objections to the Report by Plaintiff filed April 28, 1987 ("Objections"). Familiarity of the reader therewith is assumed. No objections have been filed by defendants, notice having been duly sent to each defendant by the Court by letters docketed on March 28, 1987. On review, the Court finds as follows.

Defendants have failed to answer the Complaint or move in the requisite period, or indeed to respond at any stage of the proceedings to date, and a Clerk's Certificate of Default was duly entered on June 10, 1985. The matter was referred to the Honorable Joel J. Tyler, United States Magistrate, who conducted a hearing on December 19, 1986 for the purpose of determining the amount of fair and reasonable damages sustained by plaintiff.

Plaintiff presented testimonial and documentary evidence which was fully submitted to the Magistrate on January 13, 1987, and extensively reviewed and evaluated in his Report and

Recommendation to this Court. This case, filed January 3, 1985 and remaining open more than twenty-eight months later, would seem to present a record for pendency of an uncontested matter.

The period in which to file objections to this Report closed on April 28, 1987, an extension from the original closing date of April 14th having been granted by the Court at plaintiff's request on April 13, 1987. Yet a letter and affidavit were filed by plaintiff, subsequent to the filing of his Objections, as late as May 5, 1987. The Court notes that these late submissions, regarding the accounting fees incurred by plaintiff's retention of Mr. Koren in this matter, should have been presented to the Magistrate in the normal course of the proceedings before him, and that plaintiff has certainly had ample opportunity to do so. Although Mr. Vogt has apparently been extremely dilatory in this regard, the Court will consider, where appropriate, the new information therein contained.

The Magistrate's Report determined that the plaintiff, by reason of the undisputed wrongful acts of the defendants detailed in the Report as well as the Complaint, was entitled to a total of $28,578.82 in compensatory damages, and $150,000 in punitive damages. Specifically, the Report assesses compensatory damages as follows: $6,000.00 for the January 1981 distribution; $8,897.00, for the deficient 1981 distribution; $1,938.00, for the deficient 1982 distribution; $4,648.39, for the 1981 Federal tax loss; $349.68, for the 1981 New York State tax loss; $5,438.50, for the 1982 Federal tax loss; $407.96, for the 1982 New York State tax loss; $137.90, for the 1983 New York State tax loss; and $761.39, for the 1982 Connecticut tax loss, all incurred by Plaintiff, and to be awarded with interest at the appropriate rates (*see* itemized table appearing in Report at 29-31).

In reviewing the recommendation of the Magistrate, "[t]he district judge is free to follow it or wholly to ignore it, or, if he is not satisfied, he may conduct the review in whole or in

part." *Mathews* v. *Weber,* 423 U.S. 261, 271 (1976). The authority and the responsibility to make an informed, final determination remains with the judge. *Id.*

While this Court concurs with and hereby adopts, in large measure, the within Report of the Magistrate and the assessment of damages therein contained, it must disallow the more attenuated damages not proximately caused by the wrongdoing of defendants, as explained below. Moreover, the damage award will be augmented in part, in accordance with plaintiff's Objections.

The Court interprets the sequence of events in connection with the failure to file an amended partnership tax return, described in the Magistrate's Report at 5-6, as a factual finding that on and after March 25, 1985, the date on which plaintiff discovered from his February 22, 1985 inquiry to the Internal Revenue Service ("IRS") that defendants had not filed the amended return as promised, plaintiff, a lawyer, had knowledge of this fact, as well as actual or constructive knowledge of the fact that his claim for refund would be barred by the statute of limitations after April 15, 1985. Yet he did not take it upon himself to file an amended partnership return, or amended returns for his own taxes. Particularly in view of his past dealings with defendants, and the errors and neglect they had previously demonstrated, the plaintiff knew or should have known that it was not reasonable to rely upon defendants in this regard.

We must assume that the Internal Revenue Service would have dealt honestly and fairly with Mr. Vogt had he filed his own amended return, with or without an amended partnership return, which any partner can sign. We also must assume that the IRS could and would have refunded the additional taxes which had been paid by Vogt as a result of the accounting error made by defendants. Accordingly, Mr. Vogt failed to mitigate his damages as required under New York law or, more accurately, *plaintiff's* failure to file an amended return was itself the proximate cause of the additional monetary loss. His damage award must be reduced accordingly.

The measure of damages on tort and fraud claims is the "actual pecuniary loss sustained as a direct result of the wrong." *Accusystems, Inc.* v. *Honeywell Information Systems,* 580 F.Supp. 474, 483 (S.D.N.Y. 1984). Where plaintiffs continue to act or fail to take some action which adds to their damages after being made aware of the fraudulent nature of the representations, they cannot hold defendants responsible for damages after that date. *Cf. Accusystems, Inc.* at 483. A plaintiff must show that he was injured as a direct and proximate result of his reliance on the misrepresentations of defendant. *Lehman* v. *Dow Jones & Co., Inc.,* 783 F.2d 285 (2d Cir. 1986); *Dress Shirt Sales, Inc.* v. *Hotel Martinique Associates,* 239 N.Y.S.2d 660, 663 (1963) (plaintiff must show actual pecuniary loss stemming from the fraud).

Such a direct, proximate link has not been demonstrated here. On the contrary, the failure of Mr. Vogt to file an amended return upon notice of the accounting errors, being informed that such a return had not been filed by defendants, and knowing that the statute would run on April 15, 1985, was an intervening cause responsible for the loss of his refund for the 1981 tax year. The accounting errors of the defendants in 1981 did not proximately cause the loss occasioned by the expiration of the statute of limitations in 1985. Accordingly, defendants cannot be held responsible for damages for excessive federal and state tax payments which might have been avoided by the reasonable efforts of Mr. Vogt upon being fully informed of the fraud.

Under New York law, there rests on a party seeking damages "the active duty of making reasonable exertions to render the injury as light as possible" *Wilmot* v. *State,* 344 N.Y.S.2d 350, 352-353 (1973). It is well settled that: "No recovery may be had for losses which the person injured might have prevented by reasonable efforts and expenditures" *Id.* at 353; *citing* 25 C.J.S. Damages § 33, p. 698. *See also Mayes Co.* v. *State of New York,* 277 N.Y.S.2d 393, 397 (1966) (per curiam). Interpreting the law of the State of New York, our

Court of Appeals has held, in *East Hampton Dewitt Corp.* v. *State Farm Mut. Auto. Ins. Co.*, 490 F.2d 1234 (2d Cir. 1973), that:

> "The rule is of general and widespread application that one who has been injured in person or property by the wrongful act or default of another is under a duty to make a reasonable effort to minimize the damages likely to result, and if he does not make such a reasonable effort, he will be debarred from recovering for additional damages resulting from such failure."
> *Citing Den Norske Ameriekalinje Actiesselkabet* v. *Sun Printing & Publishing Ass'n*, 226 N.Y. 1 (1919).

See also Pearlstein v. *Scudder and German*, 527 F.2d 1141 (2d Cir. 1975); *Morgan, Olmstead, Kennedy and Gardner, Inc.*, 585 F.Supp. 245 (S.D.N.Y. 1984).

Ordinarily, in the context of a trial, the burden of persuasion as to plaintiff's ability to mitigate rests with the defendant. *See Air et Chaleur, S.A.*, v. *Janeway*, 757 F.2d 489, 494-495 (2d Cir. 1985). However, the central concern in such cases appears to be the involvement of the court in the determination of damages which by their very nature would invite guesswork, and for which the relevant market information would be more readily available to defendants rather than to the court. For instance, in *Air et Chaleur*, the mitigation defense involved potential assessments of the market value of a "put" on stock and the factual issue of whether and for how much the plaintiffs could have sold the stock in the market after the breach of contract by defendant. Thus the Second Circuit left undisturbed the trial court's finding that defendant had failed to prove the opportunity to mitigate and mitigation. *Id.* at 495.

In the instant case, in contrast, we are essentially dealing with a break of causation, where the intervening cause is the failure of plaintiff to take reasonable steps to file his amended return to toll the statute of limitations. It is the plaintiff who must establish his damages at this stage of the proceedings; Mr.

Vogt has failed to demonstrate that the additional damages, occasioned by expiration of the statute of limitations, proximately flow from defendants' breach.

Moreover, the purpose of an inquest is to assess and determine the *fair* and *reasonable* damages. The general principle that plaintiff cannot simply fail to take curative action and thereby watch his damages accumulate is equally applicable in the context of an inquest, and the public policy served is no less compelling:

> ". . . this rule restricts the limits of liability for reasons of social and economic policy designed to protect and conserve the welfare and prosperity of the community as a whole . . . . Such a rule obviously comports with the social policies underlying mitigation of damages that can reasonably be avoided, and it also has the common-sense effect of preventing recovering for 'wounds which in a practical sense are self-afflicted' "
> *Morgan, Olmstead, Kennedy and Gardner, Inc.*, 585 F.Supp. 245, 248-249 (S.D.N.Y. 1984) (citations omitted).

New York law provides upon a default judgment that, unless plaintiff's claim is for a "sum certain or for a sum which can by computation be made certain", CPLR 3215(a), the court may "make an assessment or take an account or proof . . . ." CPLR 3215(b). We must remember that the failure of defendants to appear does not justify an undue windfall to a plaintiff; the interests of justice must intervene to prevent encroaching upon the rights of defendants by awarding damages which are not proximately caused by their breach and to which plaintiff is accordingly not entitled.

The analysis found in Carmody-Wait's New York Practice provides some insight as to the purpose underlying CPLR 3215(b): "The defendant in such case *may* attend, and may offer affirmative evidence upon the question of damages and in mitigation thereof, . . . for the purpose of *assisting the court in*

fixing the real damages suffered by the plaintiff" 8 Carmody-Wait 2d § 63:81, p. 741 (emphasis added); *see McClelland* v. *Climax Hosiery Mills,* 252 N.Y. 347 (1930). "In other words, the court retains its full power to require, or not to require, proof before it beyond the showing made by the affidavit or complaint, according to the needs of the particular case" 8 Carmody-Wait 2d § 63:83, p. 745-746. *See, e.g., Reynolds Securities, Inc.* v. *Underwriters Bank and Trust Company,* 406 N.Y.S.2d 743, 746-747 (1978) (an inquest was needed because the amount of plaintiff's damages was not readily ascertainable without consideration by the court of the reasonableness of the time which plaintiff permitted to elapse before making the covering purchase). Thus, the Court must assess and award only the fair and reasonable damages which it determines to have been caused by the defendants' conduct.

The Court notes that the issue of the "absence of an amended partnership return" was addressed by Mr. Vogt in his letter to the Magistrate dated September 25, 1986, at 3-5, which explanations for his failure to so file the Magistrate accepted as satisfactory and "cogent" (*See* Magistrate's Report at B, footnote 3). However, this Court does not find Mr. Vogt's reasons convincing, and concludes that plaintiff has not adequately demonstrated that it was reasonable under these circumstances not to act to limit his damages. The Court will evaluate the three reasons therein proferred by the plaintiff: the lack of the requisite authority, the requisite information, and the requisite expertise.

Plaintiff suggests that he was "not authorized" to sign tax returns on behalf of the partnership: "As Your Honor will readily appreciate, it is one thing for me to have relied on and reported on my personal tax returns the Schedule K-1 figures furnished to me by the defendant accountants, which I innocently assumed to be correct, but it would have been quite a different matter for me personally to attest under penalties of perjury to the accuracy of all the figures appearing on the partnership return and its attachments" (letter at 5). The Court can understand that Mr. Vogt felt uncomfortable signing

the partnership returns and attesting to the correctness of the figures appearing therein. However, we are dealing here with a legal concept of the duty to mitigate damages. *Any* partner can sign the partnership return; Mr. Vogt was a partner and was thus authorized under New York law to so sign. The fact that a partner's name is signed on the return shall be prima facie evidence that such partner is authorized to sign the return on behalf of the partnership. 26 U.S.C. § 6063.

As for Mr. Vogt's claim that his lack of familiarity with the other partners' Schedules K-1 or the finances of the firm precluded his filing, the Court does not believe that this is necessarily so. Even had Mr. Vogt written "unknown" in the areas of the return where applicable, the filing of such an amended return would have been sufficient to toll the statute of limitations, for one can file almost anything with the Internal Revenue Service and have it be deemed adequate at least for statute of limitation purposes.

Nor can Mr. Vogt claim that this partnership information would not be readily available to him if he chose to request it. Under the Partnership Law of New York, Mr. Vogt is entitled to access to the partnership books, and may inspect and copy any of them, subject to any special agreement between the partners not herein alleged. Partnership L. § 41; *see, e.g., United States* v. *Onassis,* 133 F.Supp. 327 (S.D.N.Y. 1955); *People* v. *Phillips,* 137 N.Y.S.2d 697 (1955). In addition, his fellow partners owe to him a legal duty to render on demand "true and full information of all things affecting the partnership", pursuant to Partnership L. § 42. Mr. Vogt does not contend that any demand for records or information was made in his behalf, much less that such demand was rejected by the partnership.

In addition, plaintiff does not allege or demonstrate that any records which were needed or desired by him could not have been obtained from the accounting firm, if that was where they were maintained, by subpoena duces tecum if necessary. Indeed, it is unclear whether there were in fact any specific documents as to which Mr. Vogt's access was restricted.

Plaintiff's final explanation, that he lacked the requisite expertise to file his partnership return, also lacks merit. Mr. Koren, who has been amply demonstrated by plaintiff in the record before the Magistrate to possess a high degree of expertise, was already in the employ of plaintiff and indeed was sufficiently familiar with the books and records of the partnership to have discovered the very errors of defendants which would have been the subject of such an amended return. It is clear that Mr. Koren was quite capable of filing an amended return.

Nor will this Court assume that IRS proceedings have now become so arcane that a member of the bar is incapable of reading the official directions and filing a return. It has always been the stated policy of the IRS that the lay person be given the opportunity and the necessary written instructions to file his or her own tax returns, including partnership returns. Numerous instruction booklets and guides have been issued for this purpose. While the statutory and financial complexities that our unfair tax code often involves are irritating, they are certainly not impossible. There is, after all, no requirement that a paid tax return preparer hold an accounting or other license, and most do not. The Court concludes as a matter of law that Mr. Vogt could have filed the amended tax returns himself.

Accordingly, the computation of damages sustained by plaintiff must be adjusted to omit the 1981 Federal income tax loss, determined by the Magistrate to be $4,648.39, the 1981 New York State income tax loss of $349.98, and the accompanying interest thereto.

It should be noted that the causation issue discussed above has no bearing on the damage award in connection with the tax returns filed by plaintiff for the 1982 and 1983 tax years, because these losses were not affected, and could not have been prevented, by the March 1985 notice. As discussed in the Magistrate's Report at 14-16, had the Schedule K-1 tax return material furnished to plaintiff by defendants in early 1982 reflected the $15,127 capital loss, plaintiff would have taken

steps to incur offsetting short-term capital gains, as he was in a position to do, and would have obtained tax-shelter income. It is reasonable to assume Mr. Vogt could and would have fully utilized the carry-over loss had he possessed this information in *1982.*

The Court also declines to disturb the Magistrate's finding of $150,000 punitive damages in this regard. Plaintiff's claim for punitive damages was based primarily upon two wrongful acts of the defendants: the deliberate exclusion of plaintiff from the 1982 distribution and the failure of defendants to file an amended partnership return with corrected Schedules K-1. The fact that defendants neglected to file the return still provides a basis for punitive damages, as found by the Magistrate at 23-29, despite plaintiff's notice on March 25, 1985 of defendants failure to so file, because the defendants did falsely represent to Mr. Vogt that they would take this action, and provided him with a spurious purported copy of an amended but unfiled Schedule K-1 soon after commencement of this litigation, with a note which was misleading in its suggestion that the amended return would be filed. Moreover, plaintiff received notice of the failure to file from the Internal Revenue Service and not from the defendants, who failed to respond to his legitimate inquiries. We agree with the Magistrate's assessment that where, as here, the accountant is apprised of an accounting error, and promises his client to take steps to correct or mitigate the error, but deliberately fails to take such steps, such behavior is grossly negligent and reckless, thereby warranting punitive damages.

Plaintiff's Objections

In his Objections to the Report of the Magistrate, plaintiff contends that the recommended award of punitive damages is inadequate, in part because the Report failed to impute the knowledge contained in the "smoking gun" memorandum, Exhibit 13, to defendants Abish and the accounting firm as a whole (Report at 7, 21-23; Objections at 14-17). The Court will infer that this memorandum, signed by the mysterious "NS", was in fact reviewed by his or her supervisors in the firm.

As agent, the actions and knowledge of "NS" must be imputed to the firm and its partners, including Mr. Abish. Such imputation is particularly reasonable where as here there is likely to have been direct supervision (Objections at 15, Tr. 231-32).

Indeed, under broad agency principles, liability may be imposed on a corporation for acts of its agents, contrary to orders and without authority, express or implied, merely because they were committed in the course of the corporation's business and were within the scope of the agent's employment. *See United States* v. *Uniroyal, Inc.*, 300 F.Supp. 84 (S.D.N.Y. 1969); *see also District 65, UAW* v. *Harper and Row Publishers, Inc.*, 576 F.Supp. 1468, 1483 (S.D.N.Y. 1983).

Accordingly, this Court concludes that Exhibit 13 establishes that the defendants were aware of the $20,000 posting error and made an adjusting entry on April 2, 1982, nearly six weeks prior to the May 14, 1982 distribution. However, upon considering this inference, as well as the restatement of defendants' misconduct and the arguments offered by plaintiff in support of a larger damage award, the sum of $150,000 assessed by the Magistrate appears to be adequate punitive damages and the Court declines to change this figure.

Mr. Vogt acknowledges that the Report is "fully in accordance with the approach plaintiff set forth in his January 1986 written submissions" as to the computation of damages for the excessive 1982 taxes paid by plaintiff; however, plaintiff now presents, for the first time, an "alternative approach" for calculating the carry-over loss (Objections at 7-9). The Court will not entertain a new method which should have been presented in the first instance to the Magistrate while he was making his extensive calculations. We conclude that these figures as presented in the Report are satisfactory and correct.

Plaintiff objects to the Magistrate's treatment of the 1982 and 1983 distributions for the purpose of determining interest for the 1982 deficiency. The Report recommended that the 1983 excess of $1,230 be set off against the 1982 deficiency of

$3,168, with prejudgment interest on the resultant $1,938 to be calculated from May 14, 1982, the date on which the earlier distribution should have been received (Report at 11). Plaintiff correctly observes that Mr. Koren had separately set forth as credit the excess portion of the 1983 distribution (para. 22 of his Declaration, Exhibit 37, p. 14), that the accounting justification for that differing treatment is not apparent, and that the effect of this alternate approach is to deprive plaintiff of 16 months of prejudgment interest on a part of the 1982 distribution to which he was entitled, from its May 14th payment date until August 24th date of the 1983 distribution (Objections at 6).

While this difference in treatment amounts to only a small sum, the Court will adopt the approach more favorable to plaintiff. Plaintiff is entitled to prejudgment interest on his claims pursuant to New York CPLR § 5001(b) from "the earliest ascertainable date the cause of action existed . . ." *Quintel Corp.* v. *Citibank, N.A.*, 606 F.Supp. 898, 913-914 (S.D.N.Y. 1985). Since plaintiff's method of calculating such interest refers back to the earlier distribution as the date on which interest begins for the larger portion of the deficiency, and the claim indisputably arose from the time of that May 14th distribution, the Court adopts plaintiff's figure as more in accordance with the equitable purpose of CPLR § 5001(b).

Accordingly, prejudgment interest will be calculated first on the 1982 deficiency of $3,168, for the period from May 14, 1982 to August 24, 1983, with a set-off of $1,230, the 1983 excess distribution, from that figure. Prejudgment interest from August 24, 1983 to the time of judgment will then be determined on the remaining deficiency.

Plaintiff requests leave to reopen the record and submit an affidavit from Mr. Koren "Attesting to the matters the Magistrate considered to be lacking", referring to the Magistrate's decision not to allow plaintiff a damage award for the accounting services of Mr. Koren, in part because "nowhere does Vogt set forth Koren's rate of compensation or detail the accounting

services rendered" (Objections at 4-5; Report at 18). Although plaintiff has been dilatory in submitting this fee information, as noted above, the Court sees no reason not to grant the requested accounting fees as presented in the Affidavit of Paul M. Koren, with accompanying invoices, duly filed with this Court on May 5, 1987. The listed fees and expenses, which total $12,223.00, constitute compensatory damages proximately caused by defendants' negligence and breach of contract. Prejudgment interest will be computed for these accounting expenses from thirty days following the respective dates they were invoiced.

In all other respects the Court hereby adopts the Magistrate's Report and Recommendation without modification. Any objections of the plaintiff not specifically referred to herein are rejected.

COMPUTATION OF DAMAGES

Element of Damages	Principal Amount	Interest Period	Rate	Prejudgment Interest to 5/13/87
(1) Federal Tax 1982	$ 5,438.50	4/15/83-5/13/87	9.0%	$ 1,995.41
(2) Connecticut Tax 1982	$ 761.39	4/15/83-5/13/87	9.0%	$ 279.36
(3) New York Tax 1982	$ 407.96	4/15/82-8/31/83	9.1%	
		9/1/83-2/29/84	9.1%(CD)	
		3/1/84-2/28/86	10.0%(CD)	
		3/1/86-2/28/86	7.9%(CD)	
		3/1/87-5/13/87	6.0%(CD)	$ 182.70
(4) New York Tax 1983	$ 137.90	4/15/84-2/28/86	10.0%(CD)	
		3/1/86-2/28/86	7.9%(CD)	
		3/1/87-5/13/87	6.0%(CD)	$ 44.29
(5) Jan. 1981 Distribution	$ 6,000.00	1/1/81-6/24/81	6.0%	
		6/25/81-5/13/87	9.0%	$ 3,348.80
(6) Deficient 1981 Distribution	$ 8,897.00	1/1/82-5/13/87	9.0%	$ 4,295.12
(7) Deficient 1982 Distribution	$ 1,938.00			$ 1,012.74
	$ (3,168.00	5/14/83-8/24/83	9.0%	
	$ 1,938.00	8/24/83-5/13/87	9.0%)	
Accounting Services				
(8) Invoice 2/25/83	$ 1,686.00	3/25/83-5/13/87	9.0%	$ 627.33
(9) Invoice 9/26/83	$ 5,180.00	10/26/83-5/13/87	9.0%	$ 1,652.77
(10) Invoice 3/21/86	$ 2,217.00	3/21/86-5/13/87	9.0%	$ 228.68
(11) Invoice 12/22/86	$ 3,140.00	1/22/87-5/13/87	9.0%	$ 85.94
TOTAL COMPENSATORY	$ 35,803.75			$13,753.14
(12) Punitive	$150,000.00			
TOTAL DAMAGES PLUS INTEREST	$199,556.89			

The Clerk shall enter judgment in favor of Plaintiff and against Defendants jointly and severally for $35,803.75 in compensatory damages, $13,753.14 in prejudgment interest, and $150,000 in punitive damages, for a total of $199,556.89.

So Ordered.

CHARLES L. BRIEANT

Charles L. Brieant
Chief U.S.D.J.

Dated: White Plains, New York
May 13, 1987

[Filed May 14, 1987]

United States District Court
Southern District of New York

WILLIAM H. VOGT III,

Plaintiff,

—against—

SHELDON ABISH,
MAHONEY, COHEN & CO., P.C.

Defendants.

85 Civil 0088-CLB

Judgment

Whereas the above entitled action having been assigned to the Honorable Charles L. Brieant, Chief, United States District Judge, and the Court thereafter on May 13, 1987, having handed down its memorandum and order adopting in large measure the Report and Recommendations of the Magistrate on damages due to the default of the defendants to answer the complaint, IT IS

ORDERED, ADJUDGED AND DECREED: That the plaintiff recover from the defendants jointly and severally the sum of $199,556.89.

Dated: May 14, 1987
White Plains, N.Y.

RAYMOND F. BURGHARDT
Clerk

United States District Court
Southern District of New York

WILLIAM H. VOGT, III,

Plaintiff,

–against–

SHELDON ABISH AND
MAHONEY, COHEN & CO., P.C.

85 Civ. 0088

July 13, 1987
2:00 P.M.

Before: Hon. Charles L. Brieant
Chief District Judge

Appearances:

VOGT & O'DONNELL
Attorneys for Plaintiff
William H. Vogt, III
Glenn Karta

STRASSBERG & STRASSBERG
Attorneys for Mahoney, Cohen
Louis Strassberg
Louis Strassberg, Jr.

PLUNKETT & JAFFE
Attorneys for Mahoney, Cohen
William Plunkett

Now the Court is going to deal with the Order to Show Cause by Mahoney, Cohen only, which the Court for convenience may refer to as MCC, and the Court notes that Abish is not moving and has never deigned to give any attention to this matter. And since he is not here it is useless for me to comment on whether he is guilty of laches.

But in any event, the defendant Mahoney, Cohen has moved to stay enforcement of the judgment against Mahoney, Cohen and has claimed lack of subject matter jurisdiction and lack of personal jurisdiction and also requested to have the judgment set aside in the interests of justice and consideration of the extraordinary circumstances claimed in the motion papers. The Court will discuss these items one at a time.

This Court does not believe that defendant Mahoney, Cohen correctly sets forth the law so as to require actual receipt by those in central control of a corporation to be necessary to effect service of process. Rule 4 imposes no requirement that service by mail physically reached those principles who regard themselves as the managerial and controlling officers of the corporation or that the shareholders owning a majority of the stock actually received the papers.

It is only necessary that the mail service reach the corporation defendant which is undisputed as what happened here and to hold otherwise would wreak havoc in our system and affect the sanctity of judgments in contravention of the purposes of Rule 4 and would create negative incentives for purported neglect and ignorance.

The Court holds that it acquired personal jurisdiction over MCC January 7, 1985, when Mahoney, Cohen received the process served by mail pursuant to Rule 4(c)(2)(C)(ii), of the Federal Rules and the Court relies on Morse against Elmira Country Club. The Plaintiff's letter to the Court dated May 30th, annexed to the motion as Exhibit G, attaches the certified mail receipt and postal return card establishing receipt of service and it is understood that that signatory is Rose Hirshberg, who was a former receptionist at the office and there is no impediment in that form of service and that is efficacious service by mail. And it is irrelevant for the purposes of Rule 4 or for consideration of the validity of the personal jurisdiction of this Court whether Mr. Abish, who was a highly placed officer of the defendant subsequently intercepted this process or whether

the mail room personnel of the defendant mistakenly gave Mr. Abish legal papers, in which he had a potential adverse interest to that of Mahoney, Cohen and Company.

If the process of the Court delivered as certified mail by the postal service did not reach Mr. Mahoney or Mr. Cohen other than through Abish, that failure was due solely to the faulty nature of the defendant's own internal procedure and a party cannot avoid service made by Rule 4 by claiming its own internal procedures were defective. Robinson versus Bantam Books, Inc. a Southern District case 49 F.R.D. 139, 140-41 (S.D.N.Y. 1970).

The ignorance of the principals resulted directly from the absence of prudent and appropriate procedures to assure that court papers would be routed directly to people in charge of the corporation's business. And the Court notes that this is not excusable neglect, an analogous class action Supermarkets General against Grinnell Corporation affirmed in 1974, by the Second Circuit treat failure to opt out of a class in the same fashion and held that the failure of internal procedures of plaintiffs to allow them to see the class action notice, reached the proper person is no excuse. There are other documents in the case which should have given timely notice to Mahoney, Cohen and Company.
An order to produce documents was addressed, sent separately to Mahoney, Cohen, addressed to its managing partner as indicated by the certified mail receipt and the postal return card.

An inference follows that this did reach the addressee and if it did not, that certainly is not a fault attributable to the plaintiff. Several certified mail postal return cards signed by Miss Hirshberg establish that MCC did in fact receive this correspondence and the Court's own letter to MCC which was gratuitously sent March 27, 1987 and issued in order to avoid a possible miscarriage of justice due to some kind of omission, appears as an exhibit to the Berry affidavit, and he attests to its receipt by MCC Mahoney, Cohen and Company.

This letter should have been sufficient to evoke the attention of the principals. The Court finds no duty imposed on the plaintiff to contact the principals of the firm personally. Service of the process of the Court and in accordance with the Federal Rules which service the Court finds to be adequately affected in this case is sufficient.

Also the Court believes it was reasonable for the plaintiff to have dealt personally only with Mr. Abish and to have served a process on Mahoney, Cohen by service on Abish. This plaintiff is not charged with notice of the fact that Abish was disloyal to the firm or incompetent insofar as its ability to receive notice is concerned.

There is some evidence that plaintiff did have contact prior to the lawsuit with Mr. Cohen who was then president and managing officer of the defendant and it is alleged here and not contradicted that Mr. Koren acting for the plaintiff, approached the managing partner of his own accounting firm Mr. Golub and was present in the room when Mr. Golub spoke to Mr. Cohen before undertaking a litigation retainer, and as a matter of professional courtesty and they told him that they were about to file suit. And while Mr. Cohen says he has no recollection of being so informed, the Court believes that this representation is more credible and more in accordance with the custom and practice in the accounting profession than not, and is inclined to believe the representation of Mr. Koren and Mr. Golub. However the Court's jurisdiction is not founded on this particular interchange.

The Court does not believe there was any showing that Abish was so adverse in his position to the position of Mahoney, Cohen as to make service upon him ineffectual to bind the principal. The Court notes that the quotation from New York Jurisprudence 2d, which was set forth in one of the early briefs in this case, is followed by further language not quoted in the defendant's brief which says in that the 3rd party dealing with an agent is not charged unless he has knowledge that a fraud has been perpetrated. There is no indication here that plaintiff knew that the plaintiff was engaged in perpetrating an independent fraudulent act on his own account, against Ma-

honey, Cohen. And it is appropriate knowledge of the agent here being imputed to the principal. There is no notice as I said earlier of any impairment or any adverse actions by Abish which is reasonably attributable to Mr. Vogt in these circumstances.

The Court relies on Arlinghaus against Ritenour in the Second Circuit in 1980, third party disclosure to an agent is not imputed to the principal when the agent is acting adversely to the principal's interest and the third party has notice of this.

The Court finds there is not sufficient evidence to justify a finding of notice. This is consistent with the Restatement of Agency (2d) Section 271. The defendant corporation has a fiduciary duty to the plaintiff and a contractual duty, and in this regard the Court notes Greene against Cuykendall, 40 N.Y. 2d 801, which would sustain the agency under these circumstances.

The Court concludes that even if the mail service was faulty, which this Court does not believe that it was, the defendant has not presented sufficient facts which would permit it to disclaim the subsequent personal service of process accepted by Mr. Abish on behalf of Mahoney, Cohen and Company.

The Court finds also that Mahoney, Cohen and Company accepted the risk of doing business in a fashion in which it did not supervise more closely the action of Sheldon Abish. And while the Court can sympathize with an employer who finds that an employee is disloyal or deceiptful, as between the Mahoney, Cohen firm which failed to supervise Abish properly and plaintiff who did not know that Abish was acting in a fashion said to be disloyal to his employer, the burden should fall on the former rather than the latter.

I think the issue of statute of limitations raised here is also without merit. I would not preclude Mahoney, Cohen from raising that in the pleadings if so advised. But, the Court concludes that a claim for professional malpractice accrues upon completion of the engagement under New York Law, relying on the Sosnow case in the Second Department in 1974, affirmed by the New York Court of Appeals. And the Court

declines to treat the 1981 portion of the work in isolation, and even if the Court would do so, if that work was not completed until the financial statements of the Watson law firm for 1981 and the partners scheduled K1 forms were distributed. This did not happen until March of 1982, and process was served within the three year statute of limitations in 1985.

Furthermore a continuous course of professional service on a specific matter will bring into effect the doctrine of continuous representation which will toll the statute of limitations in New York. And the Court relies on Cohen against Goodfriend, 642 F. Supp. 95, 1001 Eastern District case applying New York law and also the New York cases cited therein. And here the defendants managed the liquidation as fiduciaries and prepared the tax returns and continued their misrepresentation to the plaintiff, following the filing of that return up to and even after suit was instituted. And in this regard the Court is referring to the false or sham amended K1 form to toll the statute.

That was deliberate concealment on the part of Abish which the Court finds imputed to Mahoney, Cohen. Also promises to file an amended partnership return through Mr. Chew and later made through Abish occurred on January 12th, 1983 and thereafter and this Complaint was served less than two years after that.

The fraudulent nature of those promises was discovered only upon receipt of the March 25th, 1983, letter from the IRS. And New York law permits an action in fraud to be commenced within two years after the fraud was discovered which was done here.

So the Court concludes that defendants do not have an affirmative defense of the statute of limitations and the Court rejects in connection with this motion to set aside the judgment, a contention that the case is time barred. This ruling is made without prejudice to any pleadings which may subsequently be filed here except that any such pleading would have to stand the test of Rule 11.

The Court sees nothing wrong with the findings of the Magistrate about punitive damages. The corporate employer may be held punitively liable for the act of an employee if the act was authorized, ratified, approved or performed by a managerial agent.

This particular individual was a highly placed officer of the defendant and in addition Mr. Chew seems to have participated and was present when Mr. Koren inspected the Watson books at the defendant's office and discovered the posting error which the defendants have been aware of since at least April of 1982, but had been wrongfully concealed from plaintiff. So MCC has direct knowledge and not simply through Abish of the inaccuracy of the partnership return and the schedules from day one through Mr. Chew as well as through the person whose initials are N. S. who was apparently an employee of MCC.

So, the Court concludes that there was adequate basis for the punitive damages award. And there is a public interest in this type of performance and lack of familiarity and lack of proper supervision if that is what occurred here are at least as serious as MCC's failure to insure that lawsuit filed against it will come to the attention of the majority stockholders.

And the fact that Mr. Abish was having a difficult time with a major client is apparently offered as a justification or excuse, really leads to a contrary inference because if they knew he was having difficulty with a major client, that was all the more reason why they should keep watch on what he was doing. And the Court also finds that there is no merit whatever in the contention that Abish was never a person with authority to make decisions for the corporation. I think he had ample apparent, if not actual authority to do what he did and make it chargeable to his employer, and was held out to the public as a person vested with authority for the firm and at least one member of the public relied on this representation to its detriment.

So the Court finds no impairment whatever to the jurisdiction in personam or subject matter jurisdiction. The Court

thinks that there is a good faith claim made when the lawsuit was filed in excess of ten thousand dollars.

The Court would deny the motion brought by the Order to Show Cause in all respects, but for one thing and that is that the Court has concluded that Mahoney, Cohen and Company has established on this motion a meritorious partial defense which it should have the right to have considered and tried to the Court. Where a party establishes a meritorious defense to a claim adjudicated on default, and there is no significant prejudice to the other side of the case, our court liberally construes Rule 60(b) motions to promote the resolution of lawsuits on their merits rather than by default.

The Court relies on Radack in the Second Circuit in 1963, which quote a grand reservoir of equitable power to do justice is said to be available in determining whether to vacate a judgment. And the Court has consistently held this rule should be construed freely when substantial justice will be served.

This Court finds it is more likely than unlikely Mr. Vogt did receive six thousand dollars from a 1981 distribution by means of a check dated in 1981, which was in fact deposited to his bank account by somebody other than himself in the amount of six thousand dollars on December 31st, 1980. And the Court finds that it is more likely than unlikely and presents fair ground for litigation, whether that six thousand dollars is part of the twenty-seven thousand three hundred dollars in January checks cleared in December, and in accordance with the December 31, 1980 work papers.

The court can accept the fact that Mr. Vogt may not have understood this to be so at the time he was proceeding before the Magistrate. And the Court believes that we had a busy and successful lawyer here who was not an accountant, who was relying in good faith on an accounting firm which had represented his law firm for a long time. He was not required to nor expected to understand all of the refinements and niceties of the firm's internal practices with the money.

That was not his function. He was supposed to be out there practicing law. And the financial figures here viewed in the context of the time in which they occurred suggest to the Court that the plaintiff was a very hard working lawyer who was not directly concerned with the niceties of the bookkeeping in the law firm. And the Court thinks it is reasonable to conclude he more likely than not received six thousand dollars in 1980, of 1981 money in 1980.

While that is not appropriate, if the partners wanted to do it they could and in the long run there is no detriment if the plaintiff has it deposited to his account one day earlier than it should have. And the Court thinks that a trial jury could perhaps find, would be entitled to find it is more likely than unlikely that somebody at the law firm took a 1981 check and deposited it to Mr. Vogt's personal bank account on December 31st, 1980. Unfortunately the check cannot be found.

The Court is not convinced that a total search of an adequate nature has been made in these records which are in the possession of Mahoney, Cohen. But on the present motion, the evidence submitted, without making any finding of credibility which the Court should not make at this time, shows that the accounting firm has a meritorious partial defense in that the Magistrate prepared his report based on the plaintiff's good faith belief and representation to him that he failed, the plaintiff failed to receive the six thousand dollars.

In the Complaint at page 6, paragraph 12 the plaintiff alleges a distribution check in the amount of six thousand dollars which plaintiff did not receive, had been posted to his drawing account as of January, 1981.

This allegation in the Complaint was repeated throughout all submissions to the Magistrate. And this Court, it is found on Magistrate Tyler's transcript of December 19th, 1986, page 41 and at page 50 and in the affidavit of the plaintiff in support of a default judgment at page 3, and in the declaration of CPA Koren who was the plaintiff's expert. And while I think this was a good faith allegation as I said earlier, I think on a trial,

the defendant Mahoney, Cohen may well be able to establish there was no factual basis for the allegation. In addition to the six thousand dollars element of the compensatory damages awarded here, the assessment of punitive damages was founded in part upon the circumstances surrounding this six thousand dollars item. And this leads the Court to believe that in the interest of justice, this judgment should continue to be stayed as to its enforcement against Mahoney, Cohen and Company, PC and that Mahoney, Cohen and Company should be relieved from its default. The judgment should stand of record as security for anything that may ultimately be awarded in this action and the judgment should stand in full force and vigor against Abish, who the Court notes even today has taken no action in the matter and is apparently guilty of laches, so that a motion to vacate by Abish might be considered differently by the Court.

So the Court will continue the stay against enforcement of the judgment as to Mahoney, Cohen and Co. The Court will allow the defendant Mahoney, Cohen and Company to answer the Complaint within twenty days from the date herein making that Answer. The defendant must be constrained by the good faith requirements of Rule 11 which will be affected in turn by all papers and proceedings had before the Magistrate to date in this case. And the Court will then permit the matter to be tried or otherwise disposed of in accordance with the law as between the plaintiff and Mahoney, Cohen and Company PC, only.

Now the foregoing constitutes the findings of fact and conclusions of law on this motion. And if there is anything that I have not covered or anything that needs to be commented on to make a complete record so you can go forward with your litigation I'll entertain further requests to find of an oral nature.

At this time Mr. Plunkett I ought to begin with you since you carried the affirmative on this motion.

MR. PLUNKETT: Your Honor, obviously you have said a lot in a short period of time and said it very cogently. We never did get an opportunity to talk about some of the legal things. I

believe without going into it, that there are some issues here particularly on the statute of limitations.

THE COURT: I said earlier that you could file an Answer and if upon your analysis you have a good faith basis for pleading the statute as an affirmative defense you may. It certainly does not defeat the Court's jurisdiction and I really don't think it has any merit. But I think you can file a pleading if your research indicates to you I am wrong, and I might just dismiss that on motion, depending on what the further presentations were.

MR. PLUNKETT: There was also a reference to section—Restatement section 272 and I think a further research and Restatement 282 which we think is the controlling reference in the restatement would lead to a different conclusion on that. With respect to the question of where we stand right now, I think that was what your Honor was addressing his question to, the judgment.

THE COURT: I want to dispose of the motion adequately and fully. Then I'll find out where you stand right now. Is there anything—I hear what you say about the statement. The Court feels that on the totality of all these facts, service was adequate. The Court has in personam jurisdiction over your client and the Court has subject matter jurisdiction.

However the Court is impressed by the fact that you have a valid partial defense to this lawsuit arising out of the six thousand dollar item. And as I indicated to you earlier more than once, I would have denied this motion with no problem, but for the six thousand dollar item as to which I think Mr. Vogt believed in good faith at the time he brought the lawsuit that he never got the money. And I think he probably did get it. So that is worth having a lawsuit over.

If you didn't have that partial good defense to this case, I would deny your motion totally. So I'm letting the judgment stand as security and I'm permitting you to file an Answer within twenty days. And in all other respects your motion is denied.

United States District Court
Southern District of New York

WILLIAM H. VOGT III,

Plaintiff,

— against —

SHELDON ABISH and
MAHONEY, COHN & CO., P.C.

Defendants.

85 Civ.
0088-CLB

Memorandum
and
Order

Brieant, Ch. J.

The motion of defendant Mahoney Cohen & Co., P.C., by order to show cause, issued June 9, 1987, is hereby disposed of as follows:

So much of the motion which seeks to vacate as void the judgment entered on May 14, 1987 due to claimed lack of subject matter jurisdiction and lack of personal jurisdiction, is denied for the reasons set forth by the Court at the hearing held July 13, 1987. See transcript.

This Court concludes that Mahoney Cohen & Co., P.C. may have a meritorious partial defense, and that in the interests of justice it should be permitted to litigate the issues in connection therewith. Accordingly, the plaintiff is stayed and enjoined until further order of the Court, from taking any steps to enforce the judgment herein against Mahoney Cohen & Co., P.C. The plaintiff shall continue to enjoy the right to proceed to enforce the same as against defendant Sheldon Abish only, who is jointly and severally liable thereon. The judgment or such portion of it which is not collected from Sheldon Abish shall stand as security for whatever plaintiff may ultimately be adjudged to recover from Mahoney Cohen & Co., P.C., as a condition imposed by this Court to vacate the default of Mahoney Cohen & Co., P.C.

Mahoney Cohen & Co., P.C. shall serve and file its answer to the complaint within 45 days from July 13, 1987. The oral findings and conclusions of this Court, expressed at the close of the hearings held July 13, 1987 in connection with this Order to Show Cause are incorporated herein as if fully set forth as a part of this Memorandum and Order.

So Ordered.

Dated: White Plains, New York
July 17, 1987

CHARLES L. BRIEANT

Charles L. Brieant
Chief Judge

United States District Court
Southern District of New York

WILLIAM H. VOGT, III,

Plaintiff,

–against–

SHELDON ABISH and
MAHONEY, COHEN & CO. P.C.

Defendants.

July 31, 1987
10:00 A.M.

Before: Hon. Charles L. Brieant
Chief District Judge

Appearances:

VOGT & O'DONNELL
Attorneys for Plaintiff
William H. Vogt, III
Glenn Karta

PLUNKETT & JAFFE
Attorneys for Mahoney, Cohen
William F. Plunkett

MARSHALL G. KAPLAN
Attorney for Abish
Marshall G. Kaplan

The Court is assuming the absolute truth of everything set forth in the motion papers here in behalf of Mr. Abish. And the Court is assuming for the purposes of its decision that Dr. Braviti would come and testify exactly as set forth in his affidavit and on cross examination, his credibility would be in no sense impaired. And because I'm accepting these allegations

in support of the Order to Show Cause, as true, the Court finds no need to have an evidentiary hearing.

The Court concludes that even on that record, an order vacating the default judgment against the defendant Abish should not be granted. The Court is concerned with two dates in this matter. One date is January 1985, and the period shortly thereafter when Mr. Abish received actual service of process in this case which he chose to default. And the Court is also concerned with the period beginning in May in 1987, when Mr. Abish knew, that he had a May 28th—at least he knew and the Court believes an inference can be drawn that he knew when the issue first hit the Law Journal. So the Court is concerned with capacity on those particular dates. The Court concludes that at the time in 1985, when he received service of process there was no allegation that he was hospitalized or impaired in any other way.

Indeed he was working daily at his work for this firm of Mahoney, Cohen and Company. He had a highly placed position there. He was servicing clients directly. He was able to open the mail to the exclusion of the other partners in the company, and he was able to engage in ordinary day-to-day discourse in his profession and there is no evidence which shows him to be so incapacitated by alcohol or mental disease or anything else, so as to be unable to have Rule 4 service on him or have a privilege to default in litigation.

And the threshold necessary for finding this type of incapacity hear is regulated by New York law, and it is an extremely high threshold. The Court is relying on Winters against Miller in the Second Circuit applying New York law in 446(f) 2d page 65 and 68, and there the Court of Appeals notes that a finding of mental illness even by a judge or jury and commitment to a hospital does not raise even a presumption that the patient is incompetent or unable adequately to manage his affairs.

Absent a specific finding of incompetence the mental patient retains the right to sue or defend in his own name to sell

or dispose of his property to marry, draft a will and in general to manage his own affairs.

There is no evidence presented on this application which would suggest that he was impaired and all the circumstancial evidence is to the contrary because of the work he was doing the firm was letting him go out and seek clients, people that worked with him everyday, and he was engaged in a skilled profession which requires some concentration and some ability. And there is no adequate evidence of incapacity within the New York law having to do with service of process as of early 1985.

Now the Mahoney, Cohen moving papers here, which were filed in 1987, establish that Mr. Abish continued to practice as a public accountant and continued to be a principal of the firm of Mahoney, Cohen until May 28th, 1987. And the only thing that ended his relationship there on that date, was an article in the New York Law Journal which reported the decision on the Magistrate's report. And in an Abish affidavit annexed as Exhibit B to Mahoney, Cohen papers. And this was verified on May 28th, 1987, and it is perfectly lucid on its face and confirms the Court's understanding that Mr. Abish was aware of these proceedings, at least at that time and he was competent and he knew that Mahoney, Cohen had retained an attorney to seek to vacate the judgment, and he could have retained counsel himself at that time or could have appeared before the Court at that crucial time in the proceedings.

And indeed he might have shed some light on this problem of the six thousand dollar check had he chosen to do so. And in light of his affidavit here, the Court declines to draw an inference that he was so incapable in May of 1987 as to be unable to suffer a default or be unable to engage in laches and neglect in failing to move to lift this default.

The Court notes that prior to that time at least, he continued to practice his profession full time. He served on Jury duty. He proposed a settlement of this case at one point. He understood during the pendancy of this case the order to produce documents and he made efforts to select documents for

production, and therefore, in essence it is not a fair statement that he ignored all the legal processes and notes which were served upon him as Dr. Braviti's affidavit indicates.

He did comply with the Order to produce, at least after a fashion and he made an effort to dispose of the suit, and he thereby did look after his own interests at least to some extent. We further have been confronted with unrefuted affidavits of Mahoney, Cohen and allegations that rather than showing in action and in capacity during the important period in which this lawsuit was pending, Abish demonstrated substantial furtive an self interested activity by attempting apparently with remarkable success to grab hold of and conceal all the incoming papers sent to the Mahoney, Cohen firm by the Court, and by the plaintiff.

So the Court finds that there was not a degree of incapacity as shown by the circumstancial evidence and the Court finds that the laches of Abish between the period when he was confronted by Mahoney, Cohen and Company and asked to sign the affidavit which he did sign and the present day is significant seeing neglect and laches on his part.

The Court finds that the delay of this entire litigation has prejudiced the plaintiff to some degree, especially in as far as the intervening period, the banks destroyed the microfilm of a check which while it may still turn up, is rather significant to the lawsuit.

To prevail on this motion Mr. Abish would have to demonstrate in his own right that he has a meritorious defense and that his default was not willful and that the plaintiff will not be prejudiced if the motion were granted.

All these of these factors are minimal threshold requirements for an application under Rule 60 B-1. But none have been used by this defendant here, and even if these could be shown, the Court does not believe that Mr. Abish would be able to overcome his recent and indeed blatant laches, while this Court was holding the hearings as to whether Mahoney, Cohen would be permitted to appear and defend in the case which the Court reluctantly granted to Mahoney, Cohen believing that the

neglect of Abish ought to be imputed to Mahoney, Cohen, but that Mahoney, Cohen came close to presenting what might be a valid partial defense.

Accordingly the Court denies the motion in all respects for want of merit. The Court believes there is no just cause for delay and that the judgment may stand as to Mr. Abish.

However, the Court will grant to Mr. Abish a stay of any further proceedings to enforce the judgment as to Abish, or putting it differently I'll continue the precise stay which is set forth in the Order to Show Cause, dated July 27th, precisely in accordance with the order words thereof for thirty days, only in order that the defendant may if so advised apply to the Court of Appeals for the Second Circuit for a further stay in the event that he wishes to appeal this Order here today.

And the Court believes it is fair in light of the fact that it is summertime and the stay should remain in place for thirty days as to any further collection activities against Abish solely, within the words of the July 27th letter for a period of thirty days from this date so that he can apply for State pending appeal to the Court of Appeals in the Second Circuit.

And the Court declines to grant any further stay because the Court believes that the appeal would lack merit. That constitutes the Court's ruling on the motion and I thank you all for your attendance here today and if there is nothing further the Court has to cover, we will be in recess.

MR. VOGT: May I add one footnote, your Honor, as to your Honor's laches holding. I would suggest that also holds from the date that chambers sent a copy of the Magistrate's report to Abish. I believe there is a Berry affidavit in the Mahoney, Cohen submission saying it went to Mr. Abish.

THE COURT: Yes. The Court knows of its own knowledge the same letter was sent to Mahoney, Cohen and Abish. It was asserted by Mahoney, Cohen that he got their letter and took it out of the mail room. Nothing set forth herein is intended to say anything about the philosophical questions having to do with alcohol. I regard it as a laches case.

[Filed July 31, 1987]

United States District Court
Southern District of New York

WILLIAM H. VOGT III

Plaintiff,

—against—

SHELDON ABISH and
MAHONEY, COHEN & CO., P.C.

Defendants.

85 Civ. 0088 (CLB)

Ex Parte Order to Show Cause With A Stay

Upon the annexed affidavit of NARENDRA K. TRIVEDI, M.D. sworn to July 24, 1987, and the affidavit of MARSHALL G. KAPLAN, sworn to July 27, 1987, it is

NOW, on motion of MARSHALL G. KAPLAN, attorney for defendant, SHELDON ABISH,

ORDERED, that the plaintiff or his attorneys show cause before this Court at the Courthouse, located 101 East Post Road, White Plains, New York, on the 31st day of July, 1987, at 9:30 o'clock A.M. of that day or as soon thereafter as counsel can be heard, why an order should not be made vacating the default judgment heretofore entered against the defendant SHELDON ABISH on May 14, 1987 in the sum of $199,556.89 and granting to the said defendant SHELDON ABISH the opportunity to appear and answer the complaint, and for such other, further and different relief as to this Court may seem just and proper.

Motion Denied. See transcript July 31, 1987. SO ORDERED.

CHARLES BRIEANT

Ch. J.

[FILED OCTOBER 6, 1987]

United States Court of Appeals
FOR THE SECOND CIRCUIT

WILLIAM H. VOGT, III
Plaintiff-Appellant,

—against—

SHELDON ABISH and
MAHONEY, COHEN & CO., P.C.,
Defendants-Respondents.

87-7688(L) 87-7738

Docket Number

NOTICE OF MOTION

state type of motion

for dismissal of the appeal from the July 13, 1987 decision to vacate Mahoney's default.

MOTION BY: *(Name, address and tel. no. of law firm and of attorney in charge of case)*

PLUNKETT & JAFFE, P.C.-WILLIAM F. PLUNKETT, JR.
522 Fifth Avenue
New York, New York 10036
(212) 575-7772

OPPOSING COUNSEL: *(Name, address and tel. no. of law firm and of attorney in charge of case)*

VOGT & O'DONNELL-GLENN E. KARTA
707 Westchester Avenue
White Plains, New York 10604
(914) 328-0055

Has consent of opposing counsel:

A. been sought?	☒ Yes	☐ No
B. been obtained?	☐ Yes	☒ No
Has service been effected?	☒ Yes	☐ No
Is oral argument desired?	☒ Yes	☐ No

(Substantive motions only)

Requested return date: September 15, 1987
(See Second Circuit Rule 27(b))

Has argument date of appeal been set:

A. by scheduling order? ☐ Yes ☒ No

B. by firm date of argument notice? ☐ Yes ☒ No

C. If Yes, enter date: _____

Judge or agency whose order is being appealed:

CHIEF JUDGE CHARLES L. BRIEANT

Brief statement of the relief requested:

Dismissal of that branch of plaintiff's appeal which seeks review of the July 13, 1987 decision of the District Court to vacate Mahoney Cohen's default and permitted it to interpose an answer.

By: *(Signature of attorney)* Appearing for: *(Name of party)*

WILLIAM F. PLUNKETT, JR. MAHONEY, COHEN & CO., P.C.

Signed name must be printed beneath
William F. Plunkett, Jr.

Date: August 25, 1987

ORDER

Before: HON. J. EDWARD LUMBARD,
HON. FRANK X. ALTIMARI, C JJ,
HON. FRANK A. KAUFMAN, D.J.

IT IS HEREBY ORDERED that the motion be and it hereby is granted.

Elaine B. Goldsmith, Clerk

by: EDWARD J. GUARDARO

Edward J. Guardaro,
Deputy Clerk

October 6, 1987

[Filed November 30, 1987]

United States Court of Appeals
FOR THE
SECOND CIRCUIT

At a stated Term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Courthouse, in the City of New York, on the thirtieth day of November one thousand nine hundred and eighty-seven.

WILLIAM H. VOGT, III,

Plaintiff-Appellee, Cross-Appellant,

—v.—

SHELDON ABISH and MAHONEY, COHEN & CO., P.C.,

Defendants-Appellants,

MAHONEY, COHEN & CO., P.C.,

Defendant-Appellant, Cross-Appellee.

Nos. 87-7688 & 87-7738

A petition for rehearing of the October 6, 1987 order granting a motion requesting dismissal of the appeal of the July 13, 1987 district court order, containing a suggestion that the motion be reheard in banc having been filed herein by appellant William H. Vogt, III,

Upon consideration by the panel that decided the motion, it is

ORDERED that said petition for rehearing is DENIED.

It is further noted that the suggestion for rehearing the motion in banc has been transmitted to the judges of the court in regular active service and to any other judge on the panel that considered the motion and that no such judge has requested that a vote be taken thereon.

ELAINE B. GOLDSMITH

Elaine B. Goldsmith,
Clerk

[Filed February 4, 1988]

United States Court of Appeals

FOR THE

SECOND CIRCUIT

At a stated Term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse in the City of New York, on the fourth day of February one thousand nine hundred and eighty-eight.

Present:

HONORABLE WILFRED FEINBERG, *Chief Judge,*

HONORABLE WILLIAM H. TIMBERS, *Circuit Judge,*

HONORABLE AMALYA L. KEARSE, *Circuit Judge.*

WILLIAM H. VOGT, III, *Plaintiff-Appellee,* *Cross-Appellant,* —v.— SHELDON ABISH and MAHONEY COHEN & CO., P.C. *Defendants-Appellants,* MAHONEY, COHEN & CO., P.C., *Defendant-Appellant,* *Cross-Appellee.*	Nos. 87-7688, 87-7738, 87-7718

Appeal from the United States District Court for the Southern District of New York.

This cause came on to be heard on the transcript of record from the United States District Court for the Southern District of New York, and was argued by counsel.

ON CONSIDERATION WHEREOF, it is now hereby ordered, adjudged, and decreed that the matter is remanded to said District Court in accordance with the following.

Defendants Sheldon Abish and Mahoney, Cohen & Co. ("MCC") appeal, and plaintiff William H. Vogt III cross-appeals, from various decrees of the United States District Court for the Southern District of New York, Charles L. Brieant, Jr., *Chief Judge*. Because there are a number of questions concerning our jurisdiction to hear the arguments raised on the appeals and cross-appeal, and some of these questions depend on the meaning of certain actions of the district court, we remand to that court for clarification of the following matters.

1. On July 31, 1987, in denying a motion by Abish to vacate the default judgment entered against him, the court stated: "The Court believes there is no just cause for delay and that the judgment may stand as to Mr. Abish." It is unclear whether the court intended this to constitute a certification pursuant to Fed. R. Civ. P. 54(b), allowing the judgment against Abish to become final. A certification pursuant to Rule 54(b) should be accompanied by "'a brief reasoned statement' why there was 'no just reason for delay.'" *Arlinghaus v. Ritenour*, 543 F.2d 461, 464 (2d Cir. 1976) (quoting *Gumer v. Shearson, Hammil & Co.*, 516 F.2d 283, 286 (2d Cir. 1974)).

2. In proceedings held on July 13, 1987, the court placed certain restrictions on Vogt's right to execute the judgment against Abish on Abish's assets that were in the possession of MCC. It is unclear whether the court's rulings at the July 31, 1987 hearing were intended to supersede these restrictions.

We remand to the district court for clarification of the above matters. Pending such clarification, we retain jurisdiction and reserve decision on all issues raised by these appeals, including issues as to appellate jurisdiction.

WILFRED FEINBERG

Wilfred Feinberg, Chief Judge

WILLIAM H. TIMBERS

William H. Timbers, Circuit Judge

AMALYA L. KEARSE

Amalya L. Kearse, Circuit Judge

N.B. This Summary Order will not be published in the Federal Reporter and should not be cited or otherwise relied upon in unrelated cases before this or any other court.

[Filed April 19, 1988]

United States District Court
Southern District of New York

WILLIAM H. VOGT, III,

Plaintiff,

–against–

SHELDON ABISH and
MAHONEY, COHEN & CO., P.C.

Defendants.

85 Civ. 0088-CLB

Memorandum and Order

Brieant, Ch. J.

The familiarity of the reader with all prior proceedings in this extended matter must be assumed.

By an order issued February 4, 1988, and docketed in this Court on February 8, 1988, a panel of the Court of Appeals remanded the cross-appeals of all three parties to this Court for clarification of the matters noted below, retaining jurisdiction and reserving decision on all issues raised by the appeals, including issues as to appellate jurisdiction. The matters ordered to be clarified were stated by the Court of Appeals as follows:

> 1. On July 31, 1987, in denying a motion by Abish to vacate the default judgment entered against him, the court stated: "The Court believes there is no just cause for delay and that the judgment may stand as to Mr. Abish." It is unclear whether the court intended this to constitute a certification pursuant to Fed. R. Civ. P. 54(b), allowing the judgment against Abish to become final. A certification pursuant to Rule 54(b) should be accompanied by "'a brief reasoned statement' why there was 'no just

reason for delay,'" *Arlington v. Ritenour*, 543 F.2d 461, 464 (2d Cir. 1976) (quoting *Gumar v. Shearson, Hammil & Co.*, 516 F.2d 283, 286 (2d Cir. 1974)).

2. In proceedings held on July 13, 1987, the court placed certain restrictions on Vogt's right to execute the judgment against Abish on Abish's assets that were in the possession of MCC. It is unclear whether the court's rulings at the July 31, 1987 hearing were intended to supersede these restrictions.

This Court thereafter conducted a conference with counsel on Febraury 23, 1988, to ascertain their respective views as to how the District Court should resolve the issues presented by the order of the Court of Appeals dated February 4, 1988.

The attorneys for the respective participants in this litigation, which has now taken on a life of its own, agreed at that time that they would discuss the matter privately, and also informed the court that absent information to the effect that the issues had been resolved, the Court should treat the matter as fully submitted for decision as of March 7, 1988, later extended by agreement of counsel to March 14, 1988. Complicating the problem slightly is the fact that a petition for mandamus was filed in the Court of Appeals by Mr. Vogt on January 21, 1988, and that Court has apparently not yet acted thereon.

In a letter docketed March 10, 1988, attorney Kaplan, representing Mr. Abish, advised the Court that Mr. Abish was willing

a. That the judgement against him stand to abide the event of the trial between Vogt and [Mahoney, Cohen & Co.] with execution stayed also pending the event.

b. In consideration of the foregoing, Abish offered to withdraw his pending appeal and to have the action as against him severed.

c. Abish and [Mahoney, Cohen & Co.] would by separate agreement resolve all cross-claims and claims for contribution as between them.

Mr. Kaplan further advised the Court that it thereafter appeared that Abish and Mahoney, Cohen & Co., while apparently not rejecting his suggestion, "have been attempting to disentangle their professional relationship for several months and have, through separate lawyers, been trying to resolve matters completely extraneous to this proceeding. We anticipate that they will do so, but they have not done so as yet and we are reluctant to ask this court for further time in which to respond to the Court of Appeals. In any event, we do not anticipate that Vogt will consent to the foregoing as he is determined to press his mandamus." *Id.* Thereafter, Mr. Vogt advised the Court by letter docketed March 15, 1988, of his receipt of Mr. Kaplan's letter and that "there is consequently no stipulation extant for Vogt to consider joining in."

This Court does not believe that the panel of the Court of Appeals was concerned in any way with the subjective intent of the District Judge. Rather, it was concerned with resolving an apparent ambiguity in the record made by this Court in disclosing its intention concerning finality and the basis therefor. To the extent that the subjective intent of the writer is relevant, and I think it is not, this Court believed that Mahoney, Cohen & Co., whose liability in the case was derivative only, and imposed solely by the improper conduct of its agent Abish, has a valid partial defense to the claim arising out of a $6,000.00 dollar check, the existence of which Mr. Vogt still refuses to acknowledge. This information would have, if considered by the Magistrate, served to reduce considerably the punitive damages awarded, as well as the compensatory damages. The Court at the same time had little sympathy for Abish individually, whose default to appear or answer seemed to be somewhat egregious.

This Court did not then perceive that it was faced with a serious problem as to finality or appealability. There was a joint and several default judgment against Abish and Mahoney, Cohen & Co., which was final, but not appealable on the date of its entry because it was a default judgment. The only thing which could be appealable is the subsequent order granting

leave to reopen the default solely for the benefit of Mahoney, Cohen & Co., and the subsequent order denying similar relief to Mr. Abish. A procedural morass now seems to have come into being, which does no credit to our notion embodied in Rule 1, F. R. Civ. P., to the effect that all the rules "shall be construed to secure the just, speedy and inexpensive determination of every action."

It remains clear that Mr. Abish's failure to appear and answer in a timely fashion was a serious breach of the duty of a citizen to respond to judicial process, such that ordinarily should not be rewarded by relieving him from its consequences. Equally unfair and egregious was the manner in which his neglect and misconduct caused Mahoney, Cohen & Co. to be mulcted by Vogt for punitive damages based in part upon a $6,000.00 dollar payment which Vogt claimed before the Magistrate, and still claims, that he did not receive, but which the circumstantial evidence presented on the motions makes clear that he probably did receive.

Accordingly, hindsight now suggests, in this Court's continuous effort to seek a practical determination of all controversies on the merits, if I had this to do over again, I would probably stay the enforcement of the judgment as to all defendants, including Abish, allow it to remain in place as a lien to secure payment, reopen the default, and permit a full trial on the merits as to both Abish and Mahoney, Cohen & Co. At that trial, it now appears almost certain that Mahoney, Cohen & Co. and Abish could demonstrate that Vogt constructively received the $6,000.00 dollar check, which was deposited into his checking account prior to the date thereof. This being so, Mr. Vogt's compensatory damages must be recomputed with that fact in mind, and the issue of punitive damages should be reviewed *de novo* by the trier of fact, so as to bear a reasonable relationship to the actual loss suffered by Mr. Vogt as a result of Abish's deceit.

A trial jury viewing the issues of this case *de novo,* and considering Vogt's unreasonable refusal to admit that he received the benefit of the $6,000.00 dollar check, deposited in his

account, and his failure to take prompt and reasonable steps to mitigate his damages by filing an amended income tax return when he knew that he had been defrauded, is, in my judgment, highly unlikely to award any substantial amount of punitive damages.

This course of action may not be followed at this time, because the Court of Appeals has not yet ruled on the pending mandamus petition, and that Court has retained jurisdiction and reserved decision on all of the issues pending clarification as ordered on February 4, 1988.

This Court now respectfully suggests in response to its order for clarification, that the Court of Appeals should remand the entire case to the District Court for the purpose of entering a new order vacating both orders sought to be appealed from and permitting both Vogt and Mahoney, Cohen & Co. to appear and answer the complaint on the merits and try any genuine issues presented thereby *de novo*. *See,* 7 J. Moore, J. Lucas, Moore's Federal Practice ¶60.30 [2] (2d, ed, 1987). The judgment appealed from should remain of record for security but now be stayed as to its enforcement against both parties, so as to protect the rights of the plaintiff to the extent he prevails on such trial.

The foregoing constitutes this Court's response to the order of the Court of Appeals dated February 4, 1988.

So Ordered.

Dated: White Plains, New York
April 19, 1988

CHARLES L. BRIEANT

Charles L. Brieant
Chief Judge

[Filed June 2, 1988]

United States District Court
Southern District of New York

WILLIAM H. VOGT, III

Plaintiff,

—against—

SHELDON ABISH and
MAHONEY, COHEN & CO., P.C.,

Defendants.

85 Civ. 0088-CLB

Order

Brieant, Ch. J.

Upon the order of remand of the Court of Appeals, Docket Numbers 87-7688, 87-7738, 87-7718, dated May 12, 1988, and filed in this Court on May 23, 1988, and all prior proceedings herein, it is hereby ORDERED that

1. The enforcement of the judgment entered in this action on May 14, 1987 is hereby stayed as to all defendants and shall remain of record to secure such payment to plaintiff as may finally be adjudicated in this action; and

2. Defendants are each relieved of their default to answer the complaint and shall serve and file their answers and/or such other responsive pleadings permitted by law within twenty (20) days of the date of this order; and

3. The orders of this Court dated July 17, 1987 and July 31, 1987, are each vacated without prejudice; and

4. Counsel for the parties shall conduct an office conference not sooner than twenty-one (21) days and not later than forty-one (41) days from the date hereof for the purpose of resolving any necessary pre-trial discovery matters and reaching

agreement upon a scheduling order for the completion of all necessary pre-trial matters and for a trial of the action on the merits; and

5. A conference with the Court pursuant to Rule 16 F. R. Civ. P. will be conducted on Tuesday, July 19, 1988 at 9:00 a.m. in Room 31, White Plains Courthouse, or earlier on request of counsel for any party.

So Ordered.

Dated: White Plains, New York
May 24, 1988

CHARLES L. BRIEANT

Charles L. Brieant
Chief Judge

(2)

No. 88-264

Supreme Court, U.S.
FILED
SEP 9 1988
JOSEPH F. SPANIOL, JR.
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1988

WILLIAM H. VOGT III,

Petitioner,

—against—

SHELDON ABISH and
MAHONEY, COHEN & CO., P.C.,

Respondents.

BRIEF FOR RESPONDENT MAHONEY, COHEN & CO., P.C., IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

WILLIAM F. PLUNKETT, JR.*
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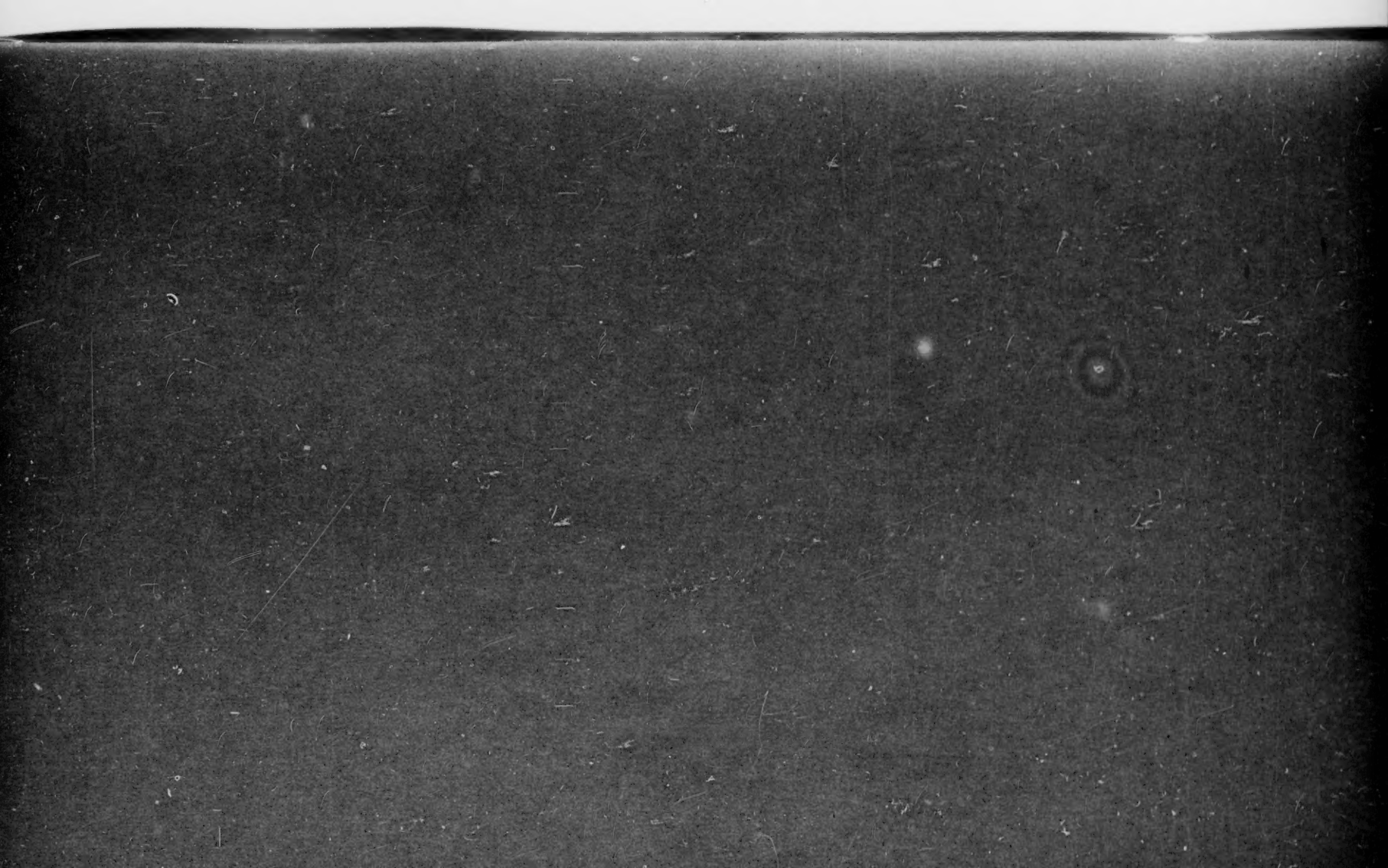
**Co-Counsel of Record for Respondent Mahoney, Cohen & Co., P.C.*

Dated: September 9, 1988



QUESTIONS PRESENTED

1. Whether the United States Court of Appeals for the Second Circuit erred in its orders (1) remanding the entire case to the district court for further proceedings as the district court deemed appropriate, and (2) denying petitioner's petition for writ of mandamus.

2. Whether the district court correctly construed the Federal Rules of Civil Procedure in vacating the default judgment against respondent Mahoney, Cohen & Co., P.C., and granting respondent Mahoney, Cohen & Co., P.C. leave to serve responsive pleadings and resolve the petitioner's claims on the merits.

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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1988

WILLIAM H. VOGT III,

PETITIONER,

-against-

SHELDON ABISH and
MAHONEY, COHEN & CO., P.C.,

RESPONDENTS.

BRIEF FOR RESPONDENT MAHONEY, COHEN & CO., P.C., IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

This brief is submitted on behalf of respondent Mahoney, Cohen & Co., P.C., in opposition to the petition for a writ of certiorari of petitioner William H. Vogt III.

U.S. SUPREME COURT REVIEW

Respondent, Mahoney, Cohen & Co., P.C. (hereinafter "MCC") does not believe that this case warrants the discretionary review of writ of certiorari. At issue is a routine order vacating a default judgment which the Second Circuit has now determined requires a trial de novo. It will be clear that there are no special or important legal issues worthy of this Court's consideration, and that the petition is a frivolous waste of the time and effort of this Court and the parties involved.

STATEMENT OF THE CASE

A. The Parties

VOGT

The petitioner, William H. Vogt III (hereinafter "Vogt") is an attorney-at-law and member of the law firm of Vogt & O'Donnell located in White Plains, New York. He is acting as his own attorney throughout the proceedings. He is formerly a partner of the law firm of Watson, Leavenworth, Kelton & Taggart (hereinafter "WLKT").

ABISH

Respondent Sheldon Abish (hereinafter "Abish") is a former officer, director, and employee of respondent MCC, a certified public accounting firm.

Abish was associated with MCC up until May 28, 1987, the date he resigned.

He was responsible for the handling of the WLKT account at MCC. In 1980, MCC became the liquidator of the WLKT partnership and this action arose from the performance of those services.

Abish was an admitted alcoholic during the fact period in question who has since undergone rehabilitation treatment. It was this illness which was a contributing factor to his failure to notify MCC of the pendency of either this dispute or of the action.

MAHONEY, COHEN & CO., P.C.

Mahoney, Cohen & Co., P.C. is a certified public accounting firm which first learned of the existence of a default judgment against it in May of 1987. It immediately took steps to ascertain the facts, vacate the default and seek resolution of the dispute on the

merits since its investigation revealed that there was at least a partial meritorious defense. The district court agreed with this position.

B. The Underlying Dispute

In the performance of its duties as liquidator of the WLKT partnership in 1980 and 1981, MCC performed various accounting services for WLKT. Certain errors were allegedly committed by Abish in the course of the performance of the accounting services with respect to the distribution of partnership funds to Vogt.

Plaintiff's complaint alleges that a twenty thousand dollar ($20,000.00) distribution error and a six thousand dollar ($6,000.00) distribution error were made to the Vogt account which, in turn, caused certain tax consequences

detrimental to Vogt. MCC has already to the satisfaction of the district court shown that Vogt received the $6000 he claimed he did not receive as a result of an MCC error, which calls into question Vogt's credibility on the other allegations.

It also calls into question whether there is any federal court jurisdiction under 28 U.S.C. 1332(a) since the actual dollar amount in controversy may be less than $10,000. Vogt allegedly made efforts to bring these errors to Abish's attention and requested him to make the necessary corrections to various drawing accounts and tax returns. Vogt asserts that these efforts were unsuccessful and that Abish, in fact, intentionally mislead Vogt into believing that amended tax returns were

filed.

Vogt took no legal action in connection with the alleged errors of Abish and MCC until January, 1985, when Vogt filed a complaint in this action.

The complaint asserts causes of action sounding in breach of contract, accountant negligence, breach of fiduciary duty and fraud. Vogt's complaint also contains a cause of action for an accounting.

Contrary to Vogt's assertion that he tried to avoid suit, Arnold Cohen, a principal of MCC, has stated that neither Vogt nor his representatives contacted Mr. Cohen nor did Vogt ever take any steps during the litigation to make sure that MCC was aware of the suit, even after default.

Service was affected by mail pursuant to F.R.Civ.P. 4(c)(2)(c)(ii) with follow-up personal service upon Abish after no acknowledgment was returned. MCC has denied it ever received service and unsuccessfully raised this defense in the district court.

No appearance was made by either Abish (who ignored the service and concealed the existence of the lawsuit from others at MCC) or MCC (because it had no actual knowledge of this action) and consequently the matter was referred to Magistrate Joel J. Tyler for an inquest to hear and report as to Vogt's money damages. With no appearance in opposition at the inquest, Vogt was awarded both compensatory and punitive damages.

C. The Report of Magistrate Tyler, the Decision and Order of the District Court and MCC's Discovery of this Lawsuit

By report and recommendation filed March 27, 1987, Magistrate Tyler recommended that a money judgment be entered against MCC and Abish in the amount of twenty-eight thousand, five hundred seventy-eight dollars and eighty-two cents ($28,578.82) in compensatory damages, and one hundred fifty thousand dollars ($150,000.00) in punitive damages. At this ex parte hearing, Magistrate Tyler took testimony from Vogt, Paul M. Koren, and Professor Joseph DiBenedetto as accounting experts. Magistrate Tyler rejected the punitive damages theory advanced by Vogt on the $20,000 posting error, finding that Abish's failure to post correctly could not be imputed to MCC.

By decision and order dated May 13, 1987, Chief Judge Charles L. Brieant essentially adopted the report while differing with the Magistrate on Vogt's theory of punitive damages, and disallowing two items of compensatory damages sought by Vogt.

Shortly after the May 13, 1987 decision and order of the district court was filed, an article appeared in The New York Law Journal on Friday, May 22, 1987 discussing this action and Chief Judge Brieant's decision. It was at this time that the principal and majority shareholders of MCC first became aware of this lawsuit. Abish, who was at that time in California, was summoned to MCC's New York office for an explanation of the events that had transpired since 1985. Abish admitted a course of conduct over

a two year period designed to avoid disclosure of the dispute and the existence of this lawsuit and resigned on May 28, 1987.

MCC promptly obtained counsel and moved for an order vacating the default judgment entered after the district court's decision of May 13, 1987.

D. MCC's F.R.Civ.P. 60(b) Motion to Vacate Its Default

By order to show cause dated June 9, 1987, Chief Judge Brieant issued an order directing plaintiff to show cause why an order should not be entered vacating the default judgment entered against MCC due to lack of personal and subject matter jurisdiction and in the interest of justice.

On July 13, 1987, after submission of papers by both sides, Chief Judge

Brieant granted MCC's motion to the extent of setting aside its default and permitting it to interpose its answer. The district court also found that it was appropriate for the judgment to remain in place and stayed any enforcement until the determination on the merits as to any liability on the part of MCC.

MCC interposed an answer pursuant to Court Order which denies many of the allegations of Vogt and cross-claims against Abish.

Subsequent to the decision vacating MCC's default, Abish appeared by counsel and moved to vacate the judgment against him. That motion was denied by the district court by memorandum and order dated July 31, 1987.

Vogt and Abish both subsequently appealed from the district court's

decisions with respect to the motions to vacate the default. MCC filed a cross-appeal. By an order issued February 4, 1988, the Second Circuit Court of Appeals remanded the cross-appeals of all three parties to the district court for clarification while retaining jurisdiction and reserving decision on all issues raised by the appeals.

Thereafter, Chief Judge Brieant issued a memorandum and order dated April 19, 1988 to the Second Circuit. In that memorandum and order, Chief Judge Brieant suggested that the court of appeals,

> "remand the entire case to the District Court for the purpose of entering a new order vacating both orders sought to be appealed from and permitting [Abish] and Mahoney, Cohen & Co., to appear and answer the complaint on the merits and try any genuine issues presented thereby de novo." (See petitioner's appendix to petition for writ of certiorari at page A-77.)

It is clear from this memorandum and order why Chief Judge Brieant found that the interests of justice require a trial de novo on the merits. MCC respectfully refers this Court to pages A-73 through A-77 of Vogt's petition for a full explanation of Chief Judge Brieant's reasons for his order.

Briefly stated, in his memorandum and order Chief Judge Brieant recognizes that Abish's neglect and misconduct caused MCC to be mulcted by Vogt for punitive damages; that the circumstantial evidence shows that Vogt received the $6000; that his refusal to admit it is unreasonable; that it was deposited in his account; that he failed to take proper and reasonable steps to mitigate his damages by filing an amended income tax return; and that these issues should

be tried de novo. The punitive damages award bears no reasonable relationship to the actual loss suffered by Vogt as a result of Abish's deceit.

The court of appeals thereafter remanded the entire case to the district court for such further proceedings as the district court deemed appropriate. [A-1 through A-2] On the same day, the court also denied, without opinion, Vogt's petition for writ of mandamus. [A-3]

REASONS FOR DENYING THE PETITION

The decision below in the court of appeals and the decisions of Chief Judge Brieant in the district court announced no novel rule of law, did not signal a conflict in the circuits, and was in all respects correct.

The decision below was fully consistent with the decisions of the court of appeals on the issue of setting aside the default of MCC and remanding the entire case to the district court for such further proceedings as the district court deemed appropriate. The Second Circuit's decision did not announce a new rule of law, address a question of first impression, signal a conflict in the circuits, or, indeed, implicate any of the other considerations normally warranting review by this Court as set forth in Rule 17 of the United States Supreme Court Rules.

Vogt now claims that the affirmance by the court of appeals of the district court's application of F.R.Civ.P. Rule 60(b) and the sound exercise of discretion by the district

court, given the circumstances embodied in the within action, constitutes grounds for review by this Court.

It is respectfully submitted that the court of appeals did not err in remanding this matter to the district court nor did the court of appeals err in denying Vogt's petition for writ of mandamus. The instant petition for writ of certiorari should be denied.

The stated basis for the remand back to the district court by the court of appeals is the memorandum and order of Chief Judge Brieant. [A-1 through A-2] In the memorandum and order, the district court, seeking to clarify an admitted "procedural morass", rendered a report to the court of appeals recommending remand. In fact, the court refers to Rule 1 of the F.R.Civ.P. and its reminder that all

the rules "shall be construed to serve the just, speedy, and inexpensive determination of every action." [A-76]

Therefore, in response to the circuit court's request for an order of clarification [A-70 through A-72], Chief Judge Brieant suggested remand of the entire case for a de novo treatment of this matter in keeping with the stated goals of Rule 1 and the unique circumstances involved herein. In order to provide Vogt with a generous measure of security in order to protect his rights to the extent he may prevail at trial, Chief Judge Brieant suggested that the judgment, which is far in excess of whatever amount Vogt would reasonably be awarded following trial, remain as security.

The court of appeals then remanded the entire case, thereby adopting the statement by Chief Judge Brieant that it would be appropriate and proper "to seek a practical determination of all controversies on the merit." [A-76]

In furtherance of that practical determination, prior to the appeal the district court found "that Mahoney, Cohen & Co., P.C., may have a meritorious partial defense, and that in the interests of justice it should be permitted to litigate the issues in connection therewith." [A-58] In support of this holding, the court noted the following:

> "The Court relies on Radack in the Second Circuit in 1963, which quote a grand reservoir of equitable power to do justice is said to be available in determining whether to vacate a judgment. And the Court has consistently held this rule

> should be construed freely when substantial justice will be served." [A-47, see transcript of July 13, 1987 hearing, at A-54]

The court's invocation of F.R.Civ.P. Rule 60(b)(6), which states that the court may set aside a judgment for "any other reason justifying relief from the operation of the judgment" represents an equitable and sound exercise of the discretionary authority available to the court in these situations.

1. Radack and the Exercise of Discretion Pursuant to Rule 60(b)(6)

In Radack v. Norwegian American Line Agency, Inc., 318 F.2d 538 (2d Cir. 1963), the court noted that Rule 60(b)(6) "gives the district court a 'grand reservoir of equitable power to do justice in a particular case.' 7 Moore, Federal Practice at p. 308 (1950 ed.),"

and further states that "the rule should be liberally construed when substantial justice will thus be served. Klapprott v. United States, 335 U.S. 601, 615, (1949)." Radack, supra, 318 F.2d at 542. See also Matarese v. LeFevre, 901 F.2d 98, 106 (2d Cir. 1986).

Further, the circuit court in Radack stated that Rule 60(b)(6) is subject "to the proper exercise of discretion by the district court considering all of the circumstances present in a given case." Id., at 543. See also, Carl Marks & Co., Inc. v. Union of Soviet Socialist Republics, 665 F.Supp. 323, 332-333 (S.D.N.Y. 1987); Dunlop v. Pan American World Airways, Inc., 672 F.2d 1044, 1051 (2d Cir. 1982); International Controls Corp. v. Vesco, 556 F.2d 665, 670 (2d Cir. 1977) ("this

discretion is especially broad under subdivision (6)").

Vogt's claims that the district court acted beyond the discretionary parameters of Rule 60(b)(6) are unavailing. The district court's sound exercise of the discretion afforded in Rule 60(b)(6) is not "an unexplained departure from [a] long line of holdings" as Vogt has stated.

On the contrary, the cases cited by Vogt in the instant petition lend support to the holding by the district court and subsequent remand by the court of appeals rather than represent an unexplained departure.

Vogt's reliance on United States v. Cerami, 563 F.2d 26 (2d Cir. 1977), is misplaced. In Cerami, supra, the circuit court notes the "extraordinary

circumstances" standard in Ackermann v. United States, 340 U.S. 193, 199 (1950), and goes on to grant the requested Rule 60(b)(6) relief in a tax dispute. In reaching that conclusion, the court noted the policy considerations applicable in vacating a judgment and stated, "we are not unmindful of other interests, among them the interest in deciding cases on their merits. These interests provide relevant parameters within which to evaluate Rule 60(b) motions; the facts give them values." (emphasis added) Cerami, 563 F.2d at 33. See also Kotlicky v. U.S. Fidelity & Guaranty Company, 817 F.2d 6, 9 (2d Cir. 1987).

This analysis was restated in the conclusion which is directly applicable to the issues herein:

> "Where one timely seeking Rule 60(b)(6) relief from a default judgment can make out a strong case

> that he had a meritorious defense which could have been asserted but for a truly extraordinary turn of events not covered by the first five clauses of the rule and which brought about his default and resulted in substantial injustice to him, it is appropriate to vacate the judgment so that the merits of his case can be considered." Id. at 35.

Davis v. Musler, 713 F.2d 907 (2d Cir. 1983), also cited by Vogt, reiterates the scope of the discretion afforded to district court in motions to vacate judgments. Citing Federal Practice and Procedure: Civil, §2693 at 471-93 (1983), the court commented that it is:

> "the trial judge, who is usually 'the person most familiar with the circumstances of the case and is in the best position to evaluate the good faith and credibility of the parties,' id. at 475, [and] is entrusted with the task of balancing these competing considerations." Davis, supra, 713 F.2d at 912.

With that guideline in place, the court then went on to decide the issue with an

analysis rooted in the facts, vacating the judgment.

Both Cerami and Davis serve to affirm the sound exercise of discretion by Chief Judge Brieant, given the unique factual situations presented, rather than exceed some murky guideline that Vogt claims exists.

Additionally, Vogt's references to Rule 55(b) and its supposed more lenient "good cause shown" standard, along with references to the case law construing that standard, are inapplicable in a consideration of the setting aside of the default judgment as to MCC pursuant to 60(b)(6) and its subsequent remand by the court of appeals.

The strongest support for the exercise of discretion by Chief Judge

Brieant can be found in the remand by the court of appeals. Surely, in light of the memorandum and order dated April 19, 1988, with its clear suggestions and stated intent, the court of appeals would not remand a matter in order to facilitate an abuse of discretion. The silence of the court of appeals in this regard speaks volumes.

It is respectfully submitted that the exercise of discretion by the district court in vacating the default as to MCC in the interest of justice was entirely proper as was the court of appeals' remand back to the district for further proceedings. It follows, therefore, that the denial of Vogt's petition for writ of mandamus was also proper.

CONCLUSION

For all of the foregoing reasons, it is respectfully submitted that the petition for certiorari must be denied.

Respectfully submitted,

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